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feature

THE LAW REGARDING VOUCHERS is in the midst of fundamental change. About a year ago, no one knew whether voucher programs could include private religious schools without running afoul of the First Amendment's establishment clause. This clause prohibits "any law respecting an Establishment of Religion" and is popularly understood to create a "wall of separation" between church and state. Today, after the Supreme Court's 2002 decision in *Zelman v. Simmons-Harris*, not only is it clear that voucher programs may include

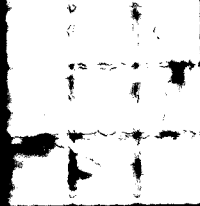
The Supreme Court will soon reconsider Washington Joshua Davey's college scholarship after he decided Will its decision render the Blaine amendments, constitutions that prohibit aid to religious schools,

THE Neutrality Principle

private religious schools, but it is quite possible that they mean. Indeed, the Supreme Court will decide a case this term, *Duney v. Leake*, which could resolve this very question. The lawsuit began when Washington State's Higher Education Coordinating Board revoked a state-funded "Promise Scholarship" from Joshua Durey, who was then a student at Northwest College, a private Christian school in Kirkland, Washington. The scholarship was available to students from low- and middle-income families who finished in the top 10 percent of their high school class and enrolled in one of the state's accredited public or private colleges. It was, in October

by JAMES E. RYAN

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to major in theology.
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unconstitutional?

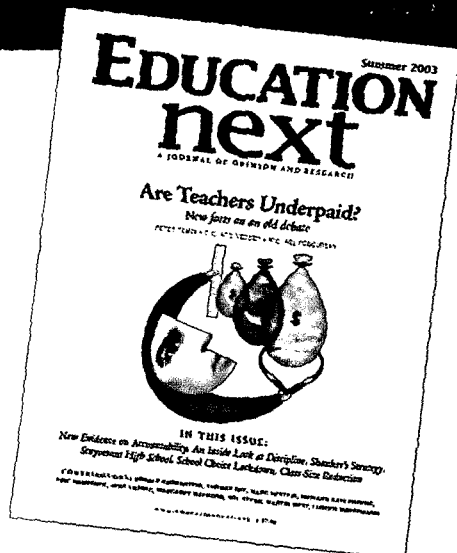


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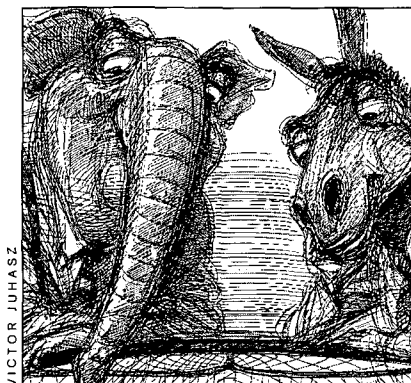
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AMERICA UNBOUND

The Bush Revolution in Foreign Policy

By Ivo H. Daalder and James M. Lindsay

When George W. Bush

peered out the window of Air Force One as it flew over Baghdad in early June, he had reason to be pleased. He had just completed a successful visit to Europe and the Middle East. The trip began in Warsaw, where he had the opportunity to personally thank Poland for being one of the two European countries to contribute troops to the Iraq War effort. He then traveled to Russia to celebrate the 300th birthday of St. Petersburg. He flew on to Évian, a city in the French Alps, to attend a summit meeting of the heads of the world's major economies. He next stopped in Sharm el Sheik, Egypt, for a meeting with moderate Arab leaders, before heading to Aqaba, Jordan, on the shore of the Red Sea to discuss the road map for peace with the Israeli and Palestinian prime ministers. He made his final stop in Doha, Qatar, where troops at U.S. Central Command greeted him with thunderous applause. Now Bush looked down on the city that American troops had seized only weeks before.

Ivo H. Daalder, a senior fellow in the Brookings Foreign Policy Studies program, and James M. Lindsay, vice-president and director of studies at the Council on Foreign Relations, are the authors of America Unbound: The Bush Revolution in Foreign Policy (Brookings, just released), from which this article is adapted.



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Bush's seven-day, six-nation trip was in many ways a victory lap to celebrate America's triumph in the Iraq War—a war that many of the leaders Bush met on his trip had opposed. But in a larger sense he and his advisers saw it as a vindication of his leadership. During his first 30 months in office, the man from Midland had started a foreign policy revolution. He had discarded many of the constraints that had bound the United States to its allies and redefined key principles that had governed American engagement in the world for more than half a century. Like most revolutions, Bush's had numerous critics. Yet he now traveled through Europe and the Middle East not as a penitent making amends but as a leader commanding respect. America unbound was remaking the course of international politics. Bush was the rare revolutionary who had succeeded. Or had he?

The Bush Revolution

What precisely was the Bush revolution in foreign policy? At its broadest level, it rested on two beliefs. The first was that in a dangerous world the best—if not the only—way to ensure America's security was to shed the constraints imposed by friends, allies, and international institutions. Maximizing America's freedom to act was essential because the unique position of the United States made it the most likely target for any country or group hostile to the West. Americans could not count on others to protect them; countries inevitably ignored threats that did not involve them. Moreover, formal arrangements would inevitably constrain the ability of the United States to make the most of its unrivaled power. Gulliver must shed the constraints that he helped the Lilliputians weave.

The second belief was that an America unbound should use its strength to change the status quo in the world. Bush did not argue that the United States keep its powder dry while it

waited for dangers to gather. Whereas John Quincy Adams—the only other son of a president later to occupy the White House—had held that the United States should not go abroad “in search of monsters to destroy,” Bush argued that America would be imperiled if it failed to do just that. “Time is not on our side,” he warned in the “Axis of Evil” speech, his 2002 State of the Union address. “I will not wait on events, while dangers gather. I will not stand by, as peril draws closer and closer. The United States of America will not permit the world's most dangerous regimes to threaten us with the world's most destructive weapons.” That logic guided the Iraq War, and it animated Bush's efforts to deal with other rogue states.

These fundamental beliefs had important consequences for the practice of American foreign policy. One was a disdain for the sorts of multinational institutions and arrangements developed by presidents from Truman through Clinton and a decided preference for the unilateral exercise of American power. Unilateralism was appealing to Bush and his advisers because it was often easier and more efficient, at least in the short term, than multilateralism. In the Kosovo war, for example, Bush and his advisers believed that the task of coordinating the views of all NATO members greatly complicated the military effort. But in the Afghanistan war, Pentagon planners did not need to subject any of their decisions to foreign approval. This is not to say that Bush flatly ruled out working with others. Rather, his preferred form of multilateralism—to be indulged when unilateral action is impossible or unwise—involved building ad hoc coalitions of the willing, or what Richard Haass, a former adviser to Colin Powell, has called “multilateralism à la carte.”

Second, preemption was no longer a last resort of American

After September 11, foreign policy wen



foreign policy. In a world in which weapons of mass destruction were spreading and terrorists and rogue states were readying to attack in unconventional ways, Bush argued in a report laying out his administration's national security strategy, "the United States can no longer solely rely on a reactive posture as we have in the past. . . . We cannot let our enemies strike first." Indeed, the United States should be prepared to act not just preemptively against imminent threats, but also preventively against potential threats. Vice President Dick Cheney was emphatic on this point in justifying the overthrow of Saddam Hussein on the eve of the Iraq War. "There's no question about who is going to prevail if there is military action. And there's no question but what it is going to be cheaper and less costly to do now than it will be to wait a year or two years or three years until he's developed even more deadly weapons, perhaps nuclear weapons."

Third, the United States should use its unprecedented power to change the regimes in rogue states. The idea of regime change was not new to American foreign policy. The Eisenhower administration engineered the overthrow of Iranian Prime Minister Mohammed Mossadegh; the CIA trained Cuban exiles in a botched bid to oust Fidel Castro; Ronald Reagan channeled aid to the Nicaraguan contras to overthrow the Sandinistas; and Bill Clinton helped Serb opposition forces get rid of Slobodan Milosevic. What was different in the Bush presidency was the willingness, even in the absence of a direct attack on the United States, to use U.S. military forces for the express purpose of toppling other governments. This was the gist of both the Afghanistan and the Iraq wars. It rested on the belief that if the United States pushed, nobody could push back.

told Japanese Prime Minister Junichiro Koizumi something similar. "History will be the judge, but it won't judge well somebody who doesn't act, somebody who just bides time here." The war on terrorism became an issue that boiled in his blood, and he intended to fight it in his fashion.

September 11 also gave Bush the opportunity to enact his revolution without fear of being challenged at home. Congressional displeasure with Bush's handling of foreign policy had grown throughout the summer of 2001. Some Democrats even thought it could be a winning issue for them in the midterm elections. In the wake of the attacks, however, congressional resistance to Bush's national security policies evaporated. Congress's deference partly reflected the enormity of the attacks and a principled belief that lawmakers should defer to strong presidential leadership in times of national crisis. But it also reflected a healthy dose of politics. Rather than blame the president for failing to anticipate the attacks, Americans rallied around him. Bush's newfound popularity translated into political power. Lawmakers may ignore the pleadings of an unpopular president, but they usually heed the demands of a popular one.

The Neoconservative Myth

By the end of the Iraq War, most commentators acknowledged that Bush had presided over a revolution in American foreign policy. They were doubtful, however, that the president was responsible for it. They instead gave the credit (or blame) to "neoconservative" thinkers within the administration, led by Deputy Secretary of Defense Paul Wolfowitz, who they said were determined to use America's great power to transform despotic regimes into liberal democracies. One writer alleged

From being a secondary priority of Bush's presidency to being its defining mission.

September 11

The Bush revolution did not start, as many have suggested, on September 11. The worldview that drove it existed long before jet planes plowed into the Twin Towers and the Pentagon. Bush outlined his philosophy while he was on the campaign trail. Most commentators failed to notice what he was saying because they were concerned more with how much he knew about the world than with what he believed. Bush began implementing his ideas as soon as he took the oath of office. His belief in the need for an America unbound was behind his pursuit of missile defense. It was also behind his rejection of the Kyoto Protocol on climate change, the International Criminal Court, and a host of other multilateral agreements he criticized or abandoned during the first eight months of his presidency.

What September 11 provided was the motive to enact the Bush revolution rapidly and without hesitation. Foreign policy went from being a secondary priority of his presidency to being its defining mission. "I'm here for a reason," Bush told his chief political adviser, Karl Rove, shortly after the attacks, "and this is going to be how we're going to be judged." He

that Bush was "the callow instrument of neoconservative ideologies." Another remarked on the "neoconservative coup" in Washington and wondered if "George W. fully understands the grand strategy that Wolfowitz and other aides are unfolding." A third thought the neoconservatives' victory was obvious. "Unless you live at the bottom of a well, you've probably noticed that 9/11 and Iraq have a transforming effect on the American Right. The short formulation is that so-called neo-conservatism has triumphed."

This conventional wisdom was wrong on at least two counts. First, it fundamentally misunderstood the intellectual currents within the Bush administration and the Republican party more generally. Neoconservatives were more prominent outside the administration, particularly in the pages of *Commentary* and the *Weekly Standard* and in the television studios of Fox News, than they were inside it. The bulk of Bush's advisers, including most notably Dick Cheney and Defense Secretary Donald Rumsfeld, were not neocons. They were instead assertive nationalists—traditional hard-line conservatives willing to use American military power to defeat threats to U.S. security but reluctant as a general rule to use American

primacy to remake the world in its image. Whereas neoconservatives talked of lengthy and expensive military occupation in Iraq, assertive nationalists spoke of a quick transition and leaving “Iraq for the Iraqis.”

Although neoconservatives and assertive nationalists differed on whether the United States should actively spread its values abroad, both were deeply skeptical of the cold war consensus on the importance of the rule of law and the relevance of international institutions to American foreign policy. They placed their faith not in diplomacy and treaties, but in power and resolve. Agreement on this key point allowed neoconservatives and assertive nationalists to form a marriage of convenience in overthrowing the cold war approach to foreign policy even as they disagreed about what kind of commitment the United States should make to rebuilding Iraq and remaking the rest of the world.

The second and more important flaw with the neoconservative coup theory was that it grossly underestimated George W. Bush. The man from Midland was not a figurehead in

at the start of the 21st century of the United States being a hyperpower, the world was beyond the ability of any one country to control. Many of the most important challenges America faced overseas could be met only with the active cooperation of others. The question was how best to secure that cooperation.

Bush maintained that if America led, friends and allies would follow. True, they might grumble because they disliked how Washington intended to lead. Some might even decide to wait until they saw the benefits of American action. In the end, however, they would join forces with the United States in combating threats such as terrorism and weapons proliferation because they trusted America’s motives and they shared its interests. Countries would not cut off their nose to spite their face.

Iraq exposed the flaw in this thinking. Most countries, including all members of the UN Security Council, shared a major interest in making sure Iraq did not possess weapons of mass destruction, especially nuclear weapons. But that com-

The lesson of Iraq, then, was that sometimes when America leads, few follow.

someone else’s revolution. He may have entered the Oval Office not knowing which general ran Pakistan, but during his first 30 months in office he was the puppeteer, not the puppet. He actively solicited the counsel of his seasoned advisers, and he tolerated if not encouraged vigorous disagreement among them. When necessary, he overruled them. George W. Bush led his own revolution.

Whither the Revolution?

Not all revolutions succeed. As Air Force One tipped its wings over Baghdad in a gesture of triumph, there were troubling signs of things to come for an America unbound. U.S. troops in Iraq found themselves embroiled in a guerrilla war with remnants of Saddam Hussein’s regime. Anger overseas at what was seen as an arrogant and hypocritical America had swelled. Close allies spoke openly not of how best to work with the United States, but of how to constrain its ability to act. Washington was beginning to confront a new question: were the costs of the Bush revolution in foreign policy about to swamp the benefits?

Part of the problem with the Bush revolution lay in how Bush and his advisers conducted it. They declined to cloak the iron fist of American power in the velvet glove of diplomacy, preferring instead to express contempt for opinions different from their own. Donald Rumsfeld, as his dismissal of France and Germany as “old Europe” attested, had a particular zeal for insulting friends and allies. Not surprisingly, this attitude struck many outside the United States—and more than a few within it—as an arrogance born of power, not principle. They resented it profoundly.

The deeper problem, however, was that the fundamental premise of the Bush revolution—that America’s security rested on an America unbound—was mistaken. For all the talk

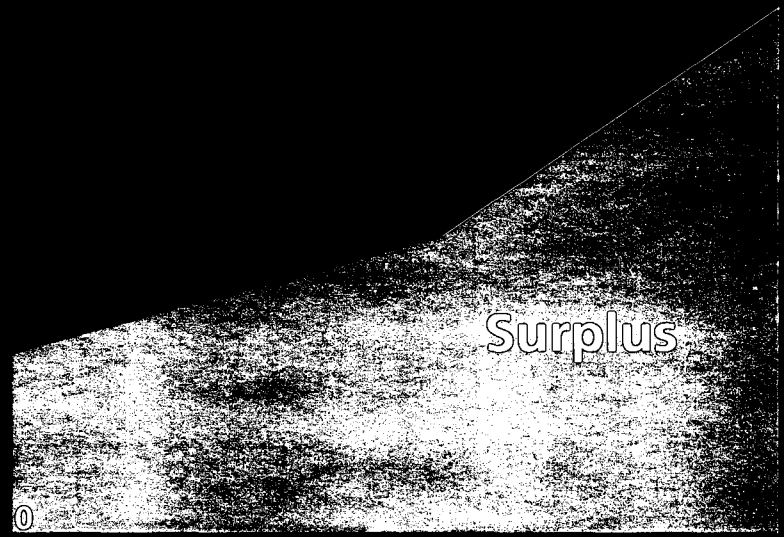
mon interest did not automatically translate into active cooperation in a war to oust Saddam Hussein—or even into support for such a war. A few countries actively tried to stop the march to war, and many others simply sat on the sidelines. Little changed after the toppling of Saddam Hussein’s statue in Firdos Square. Although many countries believed that stabilizing postwar Iraq was vitally important—for regional stability, international security, and their own national safety—they did not rush to join the reconstruction effort. In July 2003, American troops constituted more than 90 percent of all forces supporting the Iraq operation—at an annual cost to the American taxpayer of \$50 billion. Britain provided most of the other forces. The remaining foreign contributions were insignificant. Hungary, for instance, agreed to provide 133 truck drivers but no trucks, mechanics, or anything else. In other cases, countries agreed to contribute troops only after Washington agreed to pay for them—giving a whole new meaning to the concept of burden sharing.

The lesson of Iraq, then, was that sometimes when America leads, few follow. This ultimately was the real danger of the Bush revolution. America’s friends and allies seldom could stop Washington from doing as it wished, no matter how much some commentators opined to the contrary. However, America’s friends and allies did not need to resist American policy to make Washington pay a price for its desire to play unbound by any rules. They could simply refuse to come to its aid when their help was most needed or desired. That, in turn, risked undermining not only what America could achieve abroad but also domestic support at home for engaging the world. Americans could rightly ask: if others are unwilling to bear the burdens of meeting tough challenges, why should we? In that respect, an America unbound could ultimately lead to an America that is less secure. ■



ver the past two and a half years the official U.S. federal budget outlook has deteriorated in spectacular fashion. The federal budget shifted from a surplus of \$127 billion

in fiscal year 2001 to a projected deficit of about \$400 billion in fiscal 2003, which ended on September 30. This decline is due mostly to short-term factors like the economic slowdown and the war on terrorism. More ominously, the Congressional Budget Office's projected baseline budget for 2002–11 changed from a surplus of \$5.6 trillion in January 2001, when President George W. Bush took office, to a deficit of \$2.3 trillion as of August. The worsening budget projections for later in the decade are due mostly to the 2001 and 2003 tax cuts and to spending increases.



FISCAL FOLLIES

The Real Budget Problem and How to Fix It

By William G. Gale and Peter R. Orszag

William G. Gale and Peter R. Orszag are senior fellows in the Brookings Economic Studies program.

The official figures, moreover, paint far too optimistic a picture of the nation's fiscal health. The official numbers count current surpluses in the Social Security and Medicare trust funds in the budget, even though both face substantial long-term deficits. And the projections of the future make unrealistic assumptions regarding current policy.

Making more realistic assumptions about current policy and taking the Social Security and Medicare trust funds "off-budget" reveal large and persistent imbalances

10-year projections, the CBO makes three assumptions about current policy that we believe make these projections unrealistic. First, although it assumes that Congress will extend some expiring spending programs, CBO assumes that almost all temporary tax provisions will "sunset" (expire) as scheduled in the law. The 2001, 2002, and 2003 tax cuts, for example, are scheduled to sunset at various points before 2011.

Substantial sunsets in the tax code are a recent and dramatic departure from historical practice by federal policymakers intent on manipulating budget rules and hiding the true likely costs of new tax cuts. These tax sunsets, which make it possible to increase the size of annual tax cuts while staying within the budget rules, put fiscal policy on an increasingly unsustainable course, because once a tax cut is in place, Congress will be sorely tempted to extend it past its official sunset.

The alternative—not extending it—will be denounced by oppo-

maintain unless spending keeps pace with population growth too. George W. Bush endorsed the same criterion as a presidential candidate.

The third unrealistic assumption involves the alternative minimum tax (AMT), which runs parallel to the regular income tax system. Although originally designed to raise taxes on wealthy households that aggressively use tax shelters, the AMT will increasingly apply to middle-income households over the next decade, raising their tax bills and plaguing them with mind-boggling, pointless tax complexities. Unlike the ordinary income tax, the AMT is not adjusted for inflation and thus covers ever more taxpayers as prices (and incomes) rise—ensuring that policymakers will come under increasing pressure to cut back the AMT. For that reason, our projection, unlike the CBO baseline, assumes the AMT is adjusted so that the share of taxpayers who face the tax in the future is 3 percent—about the same as today.

2000

2001

2002

2003

between spending and revenues totaling about \$8 trillion over the next decade.

Worse, these deficits are projected for the decade that should be the easy time for federal finances. The first baby boomers will become eligible for Social Security in 2008 and for Medicare in 2011. The growing number of new beneficiaries, combined with lengthening life spans, technological changes that boost health care spending, and slow growth of the labor force, will place mounting pressure on federal finances in the decades to come.

Solutions to these difficulties are available, but they will be mostly unpleasant. Policymakers have not completely ignored the problems, but they have not actively sought answers either, and recent policies have made matters worse. Every year of delay makes the problems more difficult and more expensive to resolve.

What Is the Real Budget Outlook?

CBO's baseline budget is intended to be a benchmark against which legislative changes can be measured, not a prediction of likely outcomes. In making its

nents as a tax increase, a step that policymakers traditionally find distasteful, especially in election years. With President Bush and many congressional leaders already pushing to make the tax cuts permanent, it would be more realistic for the CBO baseline to assume that the tax cuts will be extended.

The second unrealistic assumption involves spending on programs that require annual appropriations decisions by Congress. The baseline assumes that such so-called discretionary spending grows each year only because of inflation. Although judgments may reasonably differ about future spending choices, we believe that current services will be difficult to

Deficit

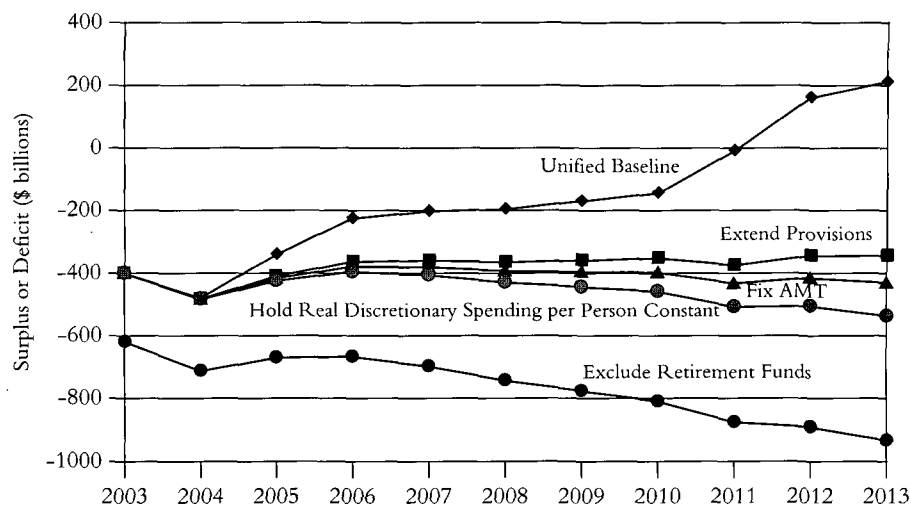
Officially, the CBO baseline projects a 10-year deficit of \$1.4 trillion for 2004 through 2013, with surpluses rising over time, as figure 1 shows. Adjusting the CBO baseline for our three assumptions regarding current policy tells quite a different story. Extending all expiring tax provisions would cost the federal budget \$2.4 trillion. Adjusting the AMT would add another \$400 billion. Adjusting discretionary spending implies another \$500 billion in outlays.

These changes leave a federal budget with a deficit of \$4.6 trillion over the next decade. Numerous uncertainties about what the future holds make it impossible to take these budget figures as exact predictions, but several basic trends are clear. First, the CBO baseline suggests that the budgetary future features rising surpluses within the 10-year window, whereas our adjusted unified budget baseline implies continual deficits through 2013, as shown in figure 1. Second, the differences grow over time. By 2013 the difference between the official projected unified budget and our alternative unified deficit is more than \$700 billion each year. Third, our adjustments, which do not include the costs of a Medicare prescription drug benefit or other new initiatives, may themselves understate the severity of the problem.

Finally, all these figures include cash-flow surpluses of \$3.2 trillion over the next decade accruing in trust funds for Social Security, Medicare, and government pensions. But—as will come as a surprise to no one—these trust funds, now in surplus, face tremendous long-term shortfalls. In various pieces of legislation between 1983 and 1990, Congress took Social Security off-budget to help clarify the state of the rest of the federal budget. We follow that approach and extend it to Medicare and government pensions. Combining this adjustment with the ones made above results in a 2004–13 projected shortfall in the nonpension portion of the budget of roughly \$7.8 trillion. Notably, this shortfall exists in every year through 2013, the end of the budget window.

That the official budget window ends in 2013 itself makes the projections misleadingly optimistic, because the budget

Figure 1.
Baseline and Adjusted Budget Outcomes, 2003–2013



outlook deteriorates rapidly thereafter. Indeed, few observers dispute that the long-term forecast involves increasing deficits as a share of the economy.

Some have lately claimed that a previously unrecognized “pot of gold” in future revenue from tax-deferred retirement accounts will be large enough to eliminate most or all of the long-term budget shortfalls. But the underlying calculations of the long-term budget shortfalls already include almost all the projected revenue from withdrawals from tax-deferred accounts. As a result, incorporating the new projections has trivial effects on the long-run budget outlook.

Are the Deficits a Problem?

None of this would matter if deficits didn’t matter, but they do. Under conventional views of how the economy operates, an increase in budget deficits (or a reduction in surpluses) will reduce future national income. This chain of events begins because the deficit reduces national saving. Theoretically, the decline in public saving represented by a budget deficit could be offset by an increase in private saving. Numerous tests, however, conclude that households do not raise saving enough to offset fully a drop in public saving induced by tax cuts.

Lower national saving, in turn, reduces national investment. Whether the fall in investment comes in the form of lower domestic investment or lower net foreign

investment by Americans, it reduces the capital stock owned by Americans and therefore diminishes the flow of future capital income received by Americans. That is, either the domestic capital stock falls or the nation is forced to mortgage some of its future capital income by borrowing from abroad. In the latter case, the foreign capital inflow may help keep domestic production at the level it would have been without the deficit, but having to repay such borrowing means that Americans will have a smaller claim on the income. Either way, Americans’ future national income is lower than it would otherwise have been. In short, deficits reduce future national income.

This is not a controversial theory. It is espoused, for example, by Federal Reserve Chairman Alan Greenspan, by the chair of President Bush’s Council of Economic Advisers, Gregory Mankiw, and by economic leaders in the earlier Clinton, Bush, and Reagan administrations.

A related concern is that the projected future budget deficits will raise interest rates. Along with many other economists, including those noted above, we believe that deficits do raise interest rates. Indeed, President Bush’s Council of Economic Advisers recently reported that a sustained deficit of 1 percent of gross domestic product would raise rates by almost one-third of a percentage point. One implication is that the Bush tax cuts will eventually raise rates by about two-thirds of a per-

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centage point—increasing payments on a \$150,000 mortgage by about \$750 a year. Another implication is that despite the reduction in marginal tax rates, the 2001 tax act raised interest rates enough to reduce investment and hurt long-term growth.

To see the real cost of long-term deficits in everyday terms, think of a family that borrows lots of money to take a vacation. It may run up its credit card balances so much that lenders charge higher interest rates on additional borrowing. But even without a higher rate, the family has a debt to repay. The borrowing effectively places a mortgage on the family's future income and thereby reduces its future living standards. The same is true for the country as a whole.

Just how much do deficits affect growth? Conventional estimates, based on models developed by CEA Chair Mankiw, indicate that the decline in the fiscal outlook since January 2001 will reduce gross domestic product in 2012 at least 1 percent and reduce national income per household in 2012 about \$2,300. The costs will grow even larger thereafter. To put it differently, controlling deficits is a pro-growth policy.

Large and persistent budget deficits may also create broader problems. As economist Edwin Truman has noted, a substantial fiscal deterioration over the longer term may cause "a loss of confidence in the orientation of U.S. economic policies and...undermine the strength of the U.S. economy and confidence in U.S. economic and financial policies." Such a loss in confidence could then put upward pressure on domestic interest rates as investors demand a higher "risk premium" on U.S. assets. Long-term deterioration in a country's fiscal position can create difficult and lasting economic problems.

Not Having a Policy Is a Policy

Policymakers face three sets of related budget challenges: near-term deficits over the next few years, medium-term deficits over the next 3–10 years, and long-term deficits thereafter.

If realistic budget projections showed rising surpluses as far as the eye could see, the near-term deficits would be no problem at all. In the presence of projected shortfalls, however, current deficits are a mixed bag. The deficits eat away at the capital stock, and the resulting costs will have to be borne over time. Nevertheless, in a slack economy, deficit spending can give the economy a needed boost, and

unusual events like the Iraq War should be at least partially funded by means of deficits.

The medium- and long-term deficits are much more troubling. Even though the economy is projected to have reached full employment within the next few years, the adjusted unified budget shows a deficit in each of the next 10 years. The disjuncture between revenues and spending indicates a fundamental imbalance persisting up to and beyond the time when baby boomers begin to retire, putting unprecedented pressure on the federal budget that will only increase over the years.

The source of the imbalance for this year is mainly a decline in revenues. Federal tax revenues in fiscal 2003 are at a generational trough of 16.5 percent of gross domestic product, the lowest share since 1959. Corporate and personal income taxes are at their lowest share of the economy since before World War II. In contrast, spending is about 20 percent of GDP in 2003, slightly less than its average since 1975.

If government leaders cannot reestablish fiscal responsibility in the remainder of this decade, it will prove far more difficult to do so after the baby boomers start retiring. The administration says that its approach to dealing with the deficit is to reduce spending and to cut taxes to make the economy grow and thereby bring in more revenue. The president asserted in his 2003 State of the Union address, "We will not deny, we will not ignore, we will not pass along our problems to other Congresses, to other presidents, and to other generations."

That rhetoric is empty at best. Leaving the problem to future generations and making the problem worse are exactly what the administration is doing. Not only is the administration raising spending, not cutting it, its tax cuts won't raise revenue—in fact, the tax cuts won't even generate much, if any, increased long-term growth.

Economic growth induced by something other than tax cuts makes the economy bigger and generates more revenue. But economic growth induced by tax cuts does not necessarily raise more revenue—the economy is bigger, yes, but a smaller tax rate applies to it. Thus, for example, if a 10 percent cut in taxes makes the economy grow 1 percent, revenues do not rise. Instead, they fall about 9 percent. Indeed, in 2001 the administration claimed that the purpose of tax cuts was to reduce the surplus. In 2003, in a remarkable turnaround, administra-

tion officials claimed that the same tax cuts, accelerated and made permanent, were needed to raise the surplus (reduce the deficit). Even the administration's own estimates show that its new rhetoric is flawed and that tax cuts do not raise revenue—consistent with estimates from Congress's Joint Committee on Taxation, the Congressional Budget Office, and every other major macroeconomic model of which we are aware.

Cutting taxes is not a way to reduce the long-term deficit—even if the tax cuts do generate more economic growth, they do not generate enough to offset their direct revenue-reducing effects. Furthermore, estimates from the CBO show that the administration's budget plans will likely have a zero or negative effect on growth. And estimates from the Joint Tax Committee show that the 2003 tax cut will likely cut jobs and growth in the long term because the adverse effect from larger budget deficits outweighs the positive effects of the tax cuts. The reductions in tax rates may increase saving, work, and investment, but the higher deficit induced by the tax cut reduces national saving and may drive up interest rates. The net effect on long-term growth, according to most studies, is negative.

Over the past several decades, national policymakers of both parties had been making a sustained push toward fiscal responsibility. Ronald Reagan agreed to income tax hikes in 1982 and 1984 as it became clear that his 1981 tax cuts, combined with increased defense spending and a slowing economy, were wreaking havoc on federal finances. In 1990, faced with continuing projected deficits, Democrats and Republicans put together a budget agreement that raised taxes, cut spending, and imposed new restrictions on spending increases and tax cuts. In 1993, with economic and fiscal problems persisting, Democrats in Congress raised taxes, cut spending, and extended the 1990 budget restrictions. That laudable recent history makes the administration's determination to ignore the underlying problems both cynical and disappointing. Rather than raise taxes and cut spending, the Bush administra-

tion has proposed spending hikes and continued tax cuts aimed at high-income families. What is needed is a return to a semblance of fiscal sanity.

An Alternative Approach

Congress and the administration can and should reduce "waste, fraud, and abuse" in spending programs and improve efforts to collect taxes that are currently unpaid. But even if these efforts are spectacularly successful, they will not resolve the underlying imbalance between projected revenues and expenditures.

Cutting spending and raising taxes are not happy alternatives, but in the end some combination of the two will be required. The fiscal problems ahead are unlike any other the country has faced in origin and nature. We will likely have to find a new way of dealing with them. In particular, the notion that federal spending can be held to its post-1980

average of about 21 percent of GDP seems impossible to maintain without either severely cutting major entitlement programs or virtually eliminating the rest of government. By 2030, spending on Social Security, Medicare, and Medicaid alone is expected to reach 14 percent of GDP—up from about 8 percent today. Even by 2013, under the adjusted budget projections noted above, balancing the budget would require a 41 percent cut in spending on Social Security and Medicare, a 47 percent cut in discretionary spending, or a 17 percent cut in all noninterest spending. Such severe cutbacks seem unlikely for political reasons and would be unattractive for economic and social reasons, unless one believes that virtually all government spending is wasteful.

The most imminent threat to fiscal sanity is the administration's proposal to make the 2001, 2002, and 2003 tax cuts permanent. The administration prefers to label Social Security and Medicare as "the real fiscal danger." But making all the temporary tax provisions in the tax code

permanent would cost \$430 billion—or 2.4 percent of GDP—in 2013 alone. Over the next 75 years, making the recent tax cuts permanent would reduce long-term revenue by more than three times the actuarial deficit in Social Security and by more than the combined deficit in Social Security and Medicare's Hospital Insurance program over the same period. By these measures, the administration's tax cuts deserve at least equal billing on the list of policies accounting for "the real fiscal danger."

In addition, legislation that boosts Medicare prescription drug benefits without simultaneously reforming the

health care system will not only dramatically raise spending but also mean missing a rare chance to reach legislative agreement on reforming Medicare.

The single most useful policy change to prevent the creation of new tax sunsets or new entitlements or the removal of existing

sunsets would be for Congress to reinstate permanently the pay-as-you-go budget rules from the 1990s. Those rules required that mandatory spending increases or tax cuts be financed by other changes in taxes or spending. Permanently reinstating those rules would require us to pay for any prescription drug benefit expansion or removal of the tax sunsets.

The bottom line is that avoiding an unsustainable explosion in government debt without destroying the role of the federal government in American society will require considerable increases in tax revenues as a share of the economy. Although some policymakers would like nothing better than to gut the role of the government, the more responsible debate should focus on how and when to raise revenue—and how to balance the required revenue increases against responsible reductions in spending. The sooner that debate begins in earnest, the more likely we will be to avoid the wrenching changes that will otherwise be necessary. ■

The bottom line is that avoiding an unsustainable explosion in government debt without destroying the role of the federal government in American society will require considerable increases in tax revenues as a share of the economy.

Economic Reform and Military Downsizing

A KEY TO SOLVING THE NORTH KOREAN NUCLEAR CRISIS?

By Michael O'Hanlon
and Mike Mochizuki

U.S. policy toward North Korea is in need of a major overhaul. Six-party negotiations in Beijing in late August did not break down, but neither did they achieve any substantive progress. Meanwhile, North Korea continues to develop a nuclear arsenal right before our eyes. We propose an ambitious plan that would get to the heart of the matter—North Korea's broken economy and other aspects of its failed society—by proposing a grand bargain to Pyongyang. North Korea would be offered a new relationship with the outside world and substantial aid if it would denuclearize, reduce military forces, and move in a direction similar to that of Vietnam and China in recent decades. If the plan failed, Washington would have a huge consolation prize—having seriously attempted diplomacy, it would then be in a much stronger position to argue to Seoul, Tokyo, and Beijing that tough measures were needed against North Korea.

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Despite some impressive successes, notably the 1994 Agreed Framework capping North Korea's nuclear activities, the Clinton policy of engagement does not offer a promising route. That approach was effective for a time but was somewhat too narrow and tactical, focusing largely on the crisis du jour. The approach appears ultimately to have encouraged in North Korea's repressive leaders a worsening habit of trying to extort resources from the international community in exchange for cutting back its dangerous weapons programs.

President Bush is impatient with this sort of attempted blackmail. But his apparent policy preference—insisting that North Korea immediately stop its nuclear activities and severely limiting talk of possible incentives to Pyongyang until it does—may fail. To date, it clearly has been failing, as the North Korean situation has changed from a serious security problem to a major crisis on his watch. North Korean leaders tend to become more intransigent when their backs are against the wall, and they are clearly willing to see their own people starve before capitulating to coercion. Pushing North Korea to the brink may also increase the odds that it will sell plutonium to the highest bidder to rescue its crumbling economy and preserve its power.

North Korea is now well into its second decade of poor economic performance, and its leaders do not seem to know what to do. They have tried modest reforms—price liberalization, special economic zones, and limited business transactions with South Koreans—with little success. They have not yet been prepared to take the risks associated with China-style economic reforms, and their instincts still push them toward high military spending. The nation's huge military force—1 million troops out of a population of 22 million—is the largest in the world in per capita terms and 10 times the global average. North Korea devotes a far greater share of gross domestic product to its armed forces than any other country, and its forces arrayed near the demilitarized zone with

South Korea are the densest concentration of firepower in the world by far.

We propose a plan that would address the nuclear weapons crisis that has so dominated headlines in recent months—and would also go much further to recast North Korea's overly militarized economy (see box on page 16). Its centerpiece would be a combination of deep conventional arms cuts, economic reform, and external economic assistance aimed at reform. President Bush himself, shortly after taking office, suggested the need for conventional arms cuts in North Korea in exchange for continued aid and diplomatic relations. Though the administration did not follow up on the president's suggestion, the idea is worth pursuing seriously. Aside from the security value of reducing North Korea's huge military presence on the Korean peninsula, a fleshed-out plan

along those lines could reduce the enormous economic burden that pushes North Korea to provoke nuclear crises to extort resources from the international community.

Our plan to prod North Korea toward demilitarization and serious economic reform and to provide the resources to give

North Korea's leaders have not been prepared to take the risks associated with China-style economic reforms.

reform a real chance offers no guarantee of success. But it also has few downsides. Failure would leave us no worse off than we are today. In fact, it would probably improve our hand in convincing South Korea, Japan, and China to adopt a tougher policy toward North Korea as needed. Success would admittedly help a totalitarian regime stay in power. But the alternatives—further economic collapse attended by misery and starvation, war, or the sale of nuclear weapons if the nation finds itself on the verge of collapse—are worse. And under our plan, the regime would be radically transformed even if it clung to power.

The Rise and Fall of the North Korean Economy

When the Korean peninsula was divided after World War II and set free from Japanese colonization, North Korea had a relatively strong economy. It boasted three-fourths of

the peninsula's mining production, at least 90 percent of its electricity generation capacity, and 80 percent of its heavy industry. The South, with a better climate, was largely an agricultural region. North Korea quickly nationalized major industries and drove up production. Its economic success probably contributed to President Kim Il Sung's confidence that he would win a war against the South, which he unleashed in 1950.

North Korea continued to outperform South Korea immediately after the war. But the seeds of its eventual economic deterioration were soon sown. It collectivized agriculture in 1953 and increasingly invested in heavy industry, much of it defense related, while turning inward and autarkic. Kim Il Sung's *juche* concept of self-reliance kept North Korea isolated from the outside world and deprived it of foreign trade.

By the late 1960s, North Korea was devoting 15–20 percent of its GDP to the military, and its economic growth gradually slowed. During the early 1970s Pyongyang tried to boost output by borrowing capital on international markets and purchasing whole factories from abroad. But oil price shocks and global stagflation thwarted that strategy. Matters thereafter went from bad to worse. The nation came to depend more and more on economic relations with the Soviet bloc, importing arms and exporting minerals, textiles, steel, and other goods. It also increased its own arms exports, largely to Iran. When the Soviet Union dissolved, North Korea lost access to most of its markets and also to subsidized Soviet oil. China provided coal and oil on favorable terms to stanch the flow of North Korean economic refugees across its borders, but even so, by the end of the decade North Korean energy resources were about half what they had been in 1990.

In the past 13 years, North Korea has suffered continuous economic contraction. GDP and per capita income have been cut roughly in half. Alternating periods of drought and flooding, together with a broken political system, have exacerbated agricultural problems. Famine has killed hundreds of thousands of North Koreans despite food aid from abroad.

Attempts at Reform

For the better part of 20 years, North Korea, like China, has shown an interest in finding a “third way” between communism and capitalism. But unlike China, it has not shown a serious commitment to reform and has achieved little success.

As its economy has worsened, North Korea has grown ever more dependent on extortion, drug trafficking, counterfeiting, whatever arms exports it can still find markets for, and cash remittances from overseas North Koreans. Its foreign trade is roughly half what it was in the 1980s. About half of all imports come from China, much of the rest from Japan and South Korea. Likewise, exports go principally to Japan, South Korea, and China. North Korea also still receives aid—mostly food and energy—averaging up to \$1 billion a year from China, South Korea, Japan, the United States, and the European Union.

Given its poor track record and the leadership's continuing communist rhetoric, North Korea's dedication to economic reform today is weak. Its leaders surely fear that liberalizing the economy could lead to political liberalization—and thus their own loss of power. Still, President Kim Jong Il, Kim Il Sung's son and successor, and other North Korean leaders seem to be searching for alternatives. Kim Jong Il has visited China at least three times since May 2000, traveled to economic centers in Beijing, Shanghai, and Shenzhen, and received briefings from Chinese economists. Korean Workers Party functionaries have also met with their Chinese counterparts to explore reform at the working level. The challenge for the United States and its chief regional allies in this matter—South Korea, Japan, and China—is to give North Koreans a push to take reform more seriously.

North Korean leaders have made three types of reforms to date. They have created special economic zones, in which they have encouraged foreign investment. They have allowed South Korean tourists to visit the North, demanding expensive surcharges for the privilege. They have also recently liberalized prices, increased wages, and begun to tolerate limited private

agriculture as well as an expansion of farmers' markets where goods can be bought and sold outside the rigidities of the command economy.

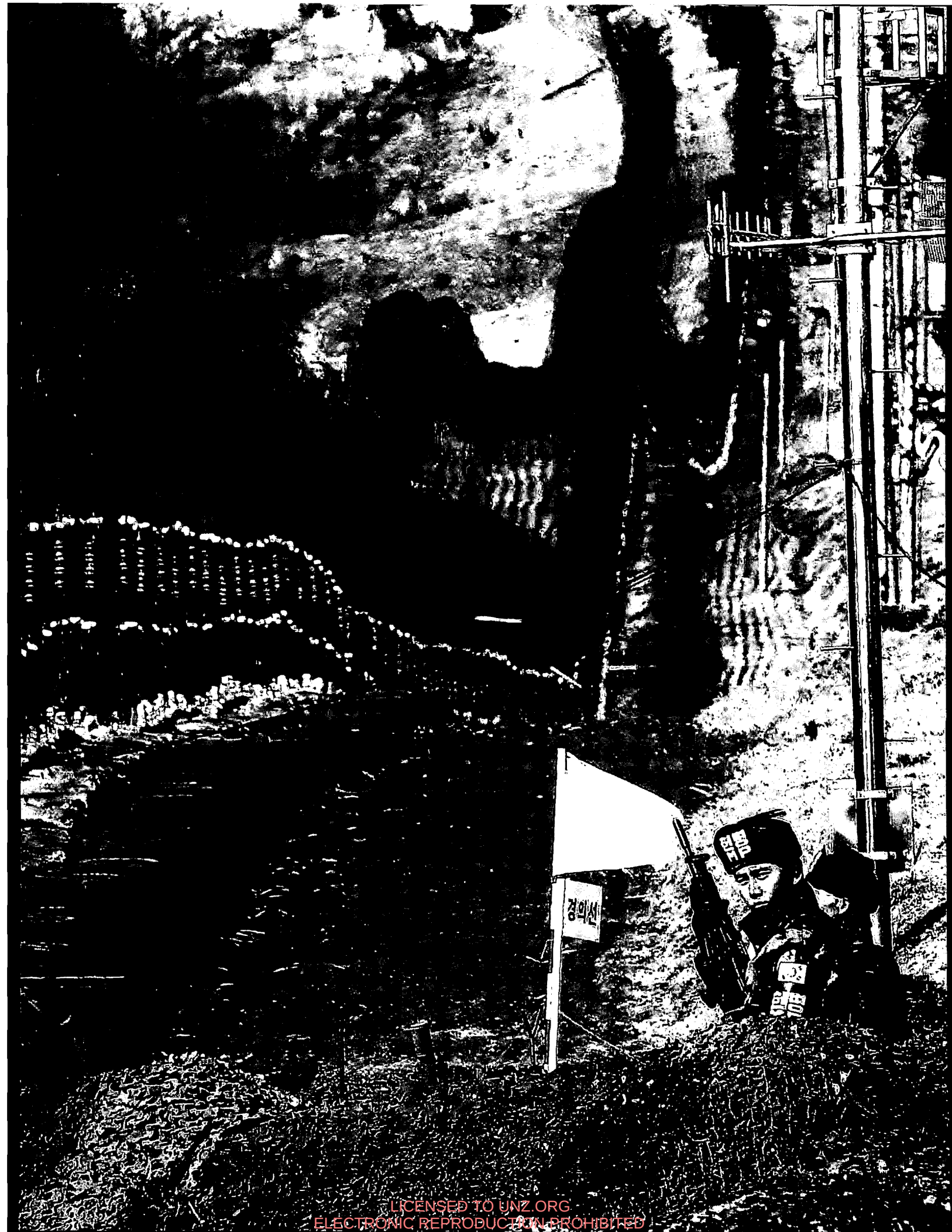
North Korea established its primary investment-oriented economic zone in the Rajin-Sonbong area, also known as the Tumen River delta, in the early 1990s. More than 700 square kilometers in area and deliberately removed from much of the rest of the country, it benefits from relatively good natural port potential. The terms granted to foreign investors here are more generous even than those granted by China and Vietnam in

their similar zones, at least on paper. Foreign firms can own all the capital invested in a given project, repatriate profits, access the region without visas, enjoy guarantees against nationalization of their assets, and possess 50-year leases on land.

So far, however, the region has yet to attract much capital. By the end of the 1990s, foreign investments totaled no more than \$34 million, and progress appears not to have accelerated. Problems include poor infrastructure, the great distances from Pyongyang and other cities, and high wage rates. Unresolved geopolitical tensions also hinder investors. Whatever the region's ultimate prospects, recent times have seen a decline in South Korean ventures in the North. Would-be foreign investors voice continued frustration with political and economic conditions in the region and the country as a whole.

In other moves to increase foreign private investment—and win desperately needed support from international financial institutions—North Korean leaders have lobbied the United States to lift trade sanctions and to remove North Korea's name from the U.S. list of state sponsors of terrorism. They have also attempted rapprochement with Japan. But these efforts too have been generally unsuccessful to date.

The challenge for the United States and its regional allies is to give North Koreans a push to take reform more seriously.



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Other reform efforts have also faltered. Although South Koreans pay up to several hundred dollars a person to visit certain important sites in North Korea, much of the cash appears to have wound up in the hands of the regime for its own uses, not for nationwide development efforts. And although in 2002 North Korea finally liberalized prices and raised wages in much of the country, the nation's distorted industrial production base, poor trade balance, and limited natural resources have hamstrung the reform move. Inflation has become severe, and some industries are reportedly unable to pay workers the promised higher wages.

Prospects for Recovery and Reform

Against this backdrop, could a serious program of economic reform buttressed by outside resources succeed?

One big plus is the nation's workforce. As its South Korean counterpart has demonstrated, Korean culture, with its emphases on hard work and group effort, is capable of remarkable things. And North Korea's population is reasonably well educated, despite heavy doses of propaganda in school and decades of isolation from the outside world. A transition period would be necessary, but on balance North Korea's human raw materials are impressive.

China's experience also provides an important model for North Korea, as its leaders seem to recognize. The PRC's ability to take an economy that Mao had largely destroyed and, without losing political power, turn it into one of the fastest-growing countries in the world must hold enormous appeal for North Korea's leaders. To be sure, reform could be harder in North Korea. China's reforms began only after Mao had departed the scene, whereas Kim still rules. China was able to accomplish many reforms by making agriculture more efficient, taking workers off the land and putting them into industrial activity. Because North Korea already has a large share of its workers in industry and a relatively small share in agriculture, its leaders would have to take workers from unproductive industry to devote to more productive nonfarm enterprises. But North Korea has available another huge source of productive manpower—its military. Downsizing its

armed forces would be a key to reform, for it would free the nation's youngest, strongest, best workers for important tasks in the years ahead.

Many economists are positive about what reform could accomplish. In *Avoiding the Apocalypse*, Marcus Noland shows that North Korea's real GDP might be expected to grow anywhere from 60 percent to almost 100 percent under various assumptions about reform. As he puts it, "There are solutions to North Korea's economic problems....The real issue is whether reform would be compatible with the continued existence of the Kim Jong Il regime...." On this latter point, Noland is agnostic, as are we. But that is no argument against proposing reform as part of a grand bargain to Pyongyang and trying to negotiate an acceptable arrangement.

Many scholars and officials in Northeast Asia have concluded that North Korea has little choice but to try such reforms. Our plan would encourage leaders in Pyongyang to get the message and act on it.

The Role of External Aid in Reform

Given the North Korean regime's apparent interest in economic reform, but uncertainty how to make it work while maintaining political control, how can outside powers play a constructive role?

Clearly no guarantees for success exist. But the downsides to trying seem few. The cost to the United States, Japan, and South Korea would be small, especially when weighed against the security implications of the likely alternatives—either a collapsing North Korea possibly willing to sell fissile materials abroad or war on the peninsula. Successful reform would gradually change North Korean society, making life better for citizens while forcing the nation's leaders to modify at least some of their ways. Failure would leave the United States no worse off than it would have been otherwise, especially since the North Korean nuclear program would have been capped in the interim in any event. (This would be a precondition to any negotiation, along with a U.S. pledge not to use force against North Korea while talks continued and a resumption of U.S. fuel oil shipments to North Korea.) Outside aid would be pro-

TERMS OF THE GRAND DIPLOMATIC BARGAIN

Seoul, Tokyo, and Washington should propose a grand diplomatic bargain that would require Pyongyang to:

- ☐ Verifiably end all its nuclear programs, allowing on-site inspections of its uranium enrichment facilities as well as inspections of suspicious sites and the plutonium at immediate issue today
- ☐ Reaffirm its commitment to allow its plutonium to be taken out of the country and to eliminate whatever nuclear weapons it now has. Ideally,

Pyongyang would agree to speed up these measures, though it might not be realistic to think it would implement them immediately

- ☐ Stop selling missiles abroad and ban all flight testing of longer-range missiles
- ☐ Let all Japanese kidnapping victims from the past few decades and their families leave North Korea
- ☐ Make large (though not unilateral) cuts in conventional forces, as well as reductions in its forward-deployed military capabilities near the demilitarized

zone. As part of the agreement, South Korea, Japan, and the United States, as well as other interested parties such as China, would keep food and fuel oil flowing on humanitarian grounds and as a show of good faith. Once the North Koreans accepted the above package, the allies would also begin to provide large amounts of economic aid. Japan would eventually provide up to \$10 billion as a form of compensation for its colonization of North Korea in the first half of the 20th century.

vided over time, rather than in a lump sum. There would be a strong presumption that the aid would continue from year to year, even in the face of setbacks in reform. But Washington and its allies would retain an unspoken leverage over Pyongyang to continue its compliance with the plan and gradually expand economic reforms. The aid efforts would serve as a form of pilot project, while also giving leaders in Pyongyang confidence that they could manage reform as it gradually spread countrywide. To the extent that North Korea allowed nationwide aid efforts and continued to support the economic reforms needed to make aid work, assistance would expand. In the first couple of years, aid would focus on improving infrastructure, mainly in the special economic zones. Implementing such projects should be relatively straightforward. Broadening the aid effort nationwide would require North Korea to accept a greater international presence on its territory and to accept more changes to its educational, agricultural, public works, and health care sectors. China could mitigate North Korean fears by providing most of the on-the-ground development experts, with funding itself coming in large measure from Japan, South Korea, and the United States. Initial success in the special economic zones might also increase North Korea's confidence in the package deal.

Above and beyond humanitarian relief and energy assistance, North Korea would probably need an average of roughly \$2 billion a year for a decade to embark on the path of economic recovery. In per capita terms—roughly \$50–\$75 a year—the total is commensurate with that given such development success stories as Taiwan and South Korea.

There is good reason to think that Japan might provide much of this assistance as a form of reparations for its colonial occupation of Korea until 1945. Japan provided \$500 million to South Korea during the 1960s; adjusting that number to account for inflation and economic growth would lead to aid in the range of \$5–\$10 billion.

Other outside assistance would also be critical. As an expression of its good faith and its commitment to improving relations, the United States would have to go beyond its current humanitarian aid, roughly \$200 million a year. It would also lift all trade sanctions and provide funds to develop North Korea's infrastructure. Its annual development aid to North Korea might reach roughly \$300 million a year. The total aid—about \$500 million annually—would be well below what it gives Israel and Egypt and roughly comparable to the amount it provides to the next tier of U.S. aid recipients—Jordan, Afghanistan, Pakistan, and Colombia. The United States, one of the least generous aid providers among the major industrial economies as a share of its national wealth, can certainly afford this expansion in aid to North Korea.

South Korea and China would clearly be critical players too. Both are already providing more aid to North Korea than the United States is. South Korea, which has largely

recovered from the 1997 Asian financial crisis, should be able to provide much more assistance under this type of radical overhaul in North-South relations. But its private sector would be the real growth engine, investing in North Korea on a major scale over time. Aid would largely lay the economic groundwork for this private investment. China would help North Korean leaders learn how to create a mixed economy that retained command features in some areas but enterprise zones in others, one that gradually carried out further price liberalization nationwide.

Prospects for Success

The prospects for this aid effort are unclear. But it has a good chance of succeeding if North Korea wants to make it work. Expectations, of course, must be reasonable—North Korea need not become another South Korea, or even another China, anytime soon. Vietnam might be a better near-term model. As first priorities, North Korea needs to fix its economy enough to take care of the basic survival needs of its people, get out of its extortionate habit of trying to use dangerous weapons programs to gain hard currency, and stop counterfeiting and drug running. More broadly, it must accept a vision for constructive engagement with the international community. By convincing Pyongyang to do so, the United States and its partners can use aid to achieve much better national security.

The benefits of the aid effort would go beyond its immediate prospects for economic success. By uniting the major powers of Northeast Asia in pursuit of a common vision for the Korean peninsula, it would harmonize the interactions of Washington, Seoul, Tokyo, and Beijing as they face the simmering nuclear crisis. These four capitals have had a difficult time uniting around any Korea policy, and their confusion and open dissension not only have hurt the prospects for collaboration but also complicate coordinating policy in case things go badly wrong and more dire measures need to be considered.

A combination of conventional force reductions and major economic reform initiatives strikes many observers as too much to add to the North Korea agenda. But more limited engagement has failed. Focusing on North Korea's nuclear program and missile programs holds little appeal for President Bush, who feels he is being blackmailed by Pyongyang's words and deeds in these areas. And without a broader reform effort, North Korea will remain a broken economy whose leaders will almost surely continue to resort to extortion—or worse—given their stark lack of alternatives for gaining hard currency.

President Bush's initial instincts that North Korea needed to reduce its threatening conventional military forces if it wished more aid and diplomatic relations with the United States were on the mark. It is time now to translate that view into a comprehensive policy proposal. ■

South
Korea's private
sector would
be the real
growth engine,
investing in
North Korea
on a major
scale over time.

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THE PERSIAN GULF

Washington Must Manage Both External Aggression and

Over the past three decades, Washington has tried a variety of approaches to ensuring the stability and security of the strategically vital Persian Gulf region. That none has been effective is evident from the fact that the United States has had to intervene directly three times in the past 16 years against regional threats—Iran in 1987–88 and Iraq in 1991 and this past spring. With the U.S. and British military success in Operation Iraqi Freedom, a broad rethinking of U.S. strategy toward the region is in order—though establishing a durable framework for Persian Gulf security is likely to be more challenging than ever. Past threats posed by Iran and Iraq were straightforward military problems amenable to solution by the vast preponderance of U.S. power. Future threats are unlikely to be as simple or discrete.

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by Kenneth M. Pollack

AHMAD AL-RUBAYE/AFP/GETTY IMAGES

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Internal Instability

It's the Oil, Stupid

America's primary interest in the Persian Gulf is ensuring the free and stable flow of the region's oil to the world at large. The issue is not whether Americans pay \$2 or \$3 a gallon for gas at the pump or whether Exxon gets contracts instead of Lukoil or even how much oil the United States imports from the Persian Gulf. The global economy built over the past 50 years rests on a foundation of inexpensive, plentiful oil. If that foundation were removed, the global economy would collapse.

Roughly 25 percent of the world's oil production comes from the Persian Gulf, with Saudi Arabia alone responsible for about 15 percent. The Persian Gulf has as much as two-thirds of the world's proven oil reserves, and its oil is absurdly economical to produce. Saudi Arabia has a majority of the world's excess production capacity, and it increases or decreases production to stabilize and control prices. The sudden loss of the Saudi oil network would send the price of oil through the ceiling, probably causing a global downturn at least as devastating as the Great Depression of the 1930s.

Washington's aim is not simply to keep oil flowing out of the Persian Gulf, but also to prevent any potentially hostile state from gaining control over the region's resources. The United States also wants to maintain military access to this geostrategically critical region to preserve its influence on events in the Middle East, Central Asia, eastern Africa, and South Asia. Finally, the United States has an interest in stamping out the terrorist groups that flourish in the region.

Triple Threat

The three main problems likely to bedevil Persian Gulf security over the next several years will be Iraq's security dilemma, Iran's nuclear weapons program, and potential internal unrest in the countries of the Gulf Cooperation Council (GCC): Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates. These problems offer no easy answers separately, let

alone together. Difficult trade-offs will have to be made.

The paradox of Iraqi power can be put simply: any Iraq that is strong enough to balance and contain Iran will be capable of overrunning Kuwait and Saudi Arabia. The recent American victory over Saddam will do little to affect this basic dynamic, which stems less from the nature of Iraq's leadership than from simple geopolitics. Like postwar Germany and Japan, post-Saddam Iraq will almost certainly be forbidden to develop weapons of mass destruction (WMD). But it will still have to protect itself from a real, albeit distant, threat from Iran, either through a credible external security guarantee or by maintaining substantial—and threatening—conventional military capabilities.

As for Iran, according to the latest estimates of U.S. intelligence and even of the International Atomic Energy Agency, its nuclear program has gone into overdrive and unless stopped—from inside or outside—is likely to produce one or more nuclear weapons within a decade. The preemptive intervention that was an option for the United States in Iraq is not an option here. Iran's population and landmass are far larger than Iraq's; its terrain would make military operations a logistical nightmare; and its people have generally rallied around the regime in the face of foreign threats. Invading Iran would be unthinkable in all but the most extraordinary circumstances.

Of course, the Iranian nuclear problem may solve itself. The Iranian people are deeply unhappy with the reactionary clerics who cling to power in Tehran, and since 1997 they have voted consistently and overwhelmingly against the hard-liners. Moreover, Iran's population is young, and the Iranian youth most strongly oppose the current regime and favor a more democratic system of government. Thus time is on the side of Iran's reformers, most of whom have expressed an interest in good relations with the United States.

All this matters because although Washington preaches a policy of universal nuclear nonproliferation, in practice it has consistently, and probably cor-

rectly, been much more concerned with proliferation by its enemies, such as Iraq and North Korea, than by its friends, such as Israel. U.S. fears about Iran's nuclear program might well diminish with the emergence of a pluralist and pro-American government in Tehran—though even then Iranian nuclear advances would cause a major headache because of their inevitable effects on proliferation elsewhere in the region.

The problem is that no one can be certain that the reformers will triumph in Iran or, if so, when. The United States must therefore assume that Iran will acquire nuclear weapons while its hard-line clerics are still in power. But the very U.S. actions called for in those circumstances—continued diplomatic and economic pressure, an aggressive military posture on Iran's borders, even threats to use force—could play into the hands of Iran's hard-liners, who maintain power in part by stoking popular fears that the United States seeks to control the country. The Iranian paradox is that preparing to deal with the worst-case scenario of Iranian hard-liners possessing nuclear weapons might very well make that scenario more likely.

Tehran appears to want nuclear weapons principally to deter an Ameri-

ian issue arouses great popular concern, but it is the failure of Arab economic and political systems that creates fertile ground for domestic insurrection or the recruitment efforts of radical Islamist groups such as al Qaeda. Too many Arabs feel powerless and humiliated by despotic governments that do less and less for them while giving them no say in their own governance. And too many feel both threatened and stifled within a society that cannot come to grips with modernity.

Most Middle East experts think that a revolution or civil war in any of the GCC states within the next few years is unlikely, but few say so now as confidently as they once did. Indeed, fears of mounting internal turmoil have prompted each of the GCC regimes to announce democratic and economic reform packages over the past 10 years. If the reforms fail and violence ensues, Washington might face some difficult security challenges. Widespread unrest in Saudi Arabia, for example, would threaten Saudi oil exports just as surely as would an Iranian invasion.

The best way for the United States to address the rise of terrorism and the threat of internal instability in Saudi Arabia and the other GCC states would be

Invading Iran would be unthinkable if

can attack. Once it gets them, however, it might be emboldened to pursue a more aggressive foreign policy. Iran's military is too weak to contemplate invading its neighbors, so the risk is more that Iran would try to shut down tanker traffic in the Strait of Hormuz to blackmail them or foment insurrection. But the U.S. security posture that would best deter Iranian aggression—a heavy presence of forces throughout the Persian Gulf—is the worst option in dealing with the third problem, terrorism and internal instability in the states of the GCC.

Terrorism and internal unrest in the Persian Gulf are ultimately fueled by the political, economic, and social stagnation of the local Arab states. American policies anger many Arabs, and the Palestin-

to reduce dramatically its military presence in the region, even to withdraw entirely. The heavy presence of U.S. troops fuels the terrorists' propaganda claims and is a humiliating reminder that the descendants of the great Islamic empires can no longer defend themselves and must answer to infidel powers. So pulling back would ease the internal pressure on the regimes and help them enact vital but painful reforms. But, as noted, a withdrawal would be the worst move from the perspective of deterring and containing Iran.

These paradoxes make finding a workable new security architecture for the Persian Gulf excruciatingly difficult. Iraq must be kept strong but not too strong. Iran must be kept in check while being pushed to liberalize. The GCC

governments must be given breathing room for reform but still be protected from their external and internal enemies. Efforts to balance these various interests, threats, and constraints may well fail, as past U.S. regional strategies have. Still, the situation is not entirely hopeless. Perhaps no perfect policy will secure every interest and counter every threat while avoiding all the strategic, political, and cultural minefields. But three broad approaches—pulling back “over the horizon,” trying to form a local NATO-like defense pact, or trying to establish a security condominium—have enough merit to be considered seriously.

Back over the Horizon

The most conservative approach to Persian Gulf security would be to pull most of America’s forces back “over the horizon.” When Washington last tried that posture—during the 1970s and 1980s—it failed because both Iran and Iraq were quite strong. Today, however, both are much weaker and likely to remain so, at least until Iran acquires nuclear weapons. Washington, meanwhile, has repeatedly demonstrated its willingness to intervene in the Gulf to protect its interests and prevent aggression. So the strategy might work better today.

On the political level, the United States would preserve its informal relationships with the GCC states and possibly add a similar association with a friendly new Iraqi government. It would make clear that any Iranian aggression would be met by an American military response. And it would continue to urge Europe, Japan, and Russia to pressure Iran to end its support for terror and its unconventional weapons programs.

The pullback would go far to alleviate the region’s internal problems and is, not surprisingly, the strategy that the Gulf Arabs favor. With Saddam gone, their overriding goal now is to minimize domestic discontent, and they believe that the United States can keep peace in the region with a minimal presence. But their enthusiasm for this strategy ought to give American planners pause. With the exception of Kuwait after the Iraqi invasion, most of these countries have shown a distressing determination over the years to ignore their problems, both external and internal, rather than confront them. Although a U.S. pullback could give them the leeway they need to push through reforms, they are equally likely to see it as a panacea for all their problems and decide that internal reforms

A Middle Eastern NATO

A second strategy for securing the Persian Gulf would be a new regional defense alliance along the lines of NATO—though this approach too has been tried unsuccessfully. In 1954, the United States convinced Iran, Iraq, Pakistan, Turkey, and the United Kingdom to sign the Baghdad Pact, pledging them to mutual defense. Four years later, Iraq withdrew, leaving Iran, Pakistan, and Turkey to form the Central Treaty Organization, which became little more than a vehicle for the United States to arm the shah of Iran. The alliances performed poorly because their members had widely divergent security problems—and because revolution in Iraq in 1958 and in Iran in 1979 knocked out the central players. Today members of a defensive alliance would have a similar view of the security problem.

The alliance would include the United States, the GCC states, and a new government of Iraq. To paraphrase Lord Ismay’s famous quip about NATO, the goal would be to keep the Americans in, the Iranians out, and the Iraqis down. A formal defense pledge would lock in an unflinching American commitment to regional security, deter outright Iranian aggression, and solve Baghdad’s security dilemma, providing a benign framework for Iraq’s conven-

..l but the most extraordinary circumstances.

In this approach, the United States would leave only the bare minimum of its current forces in place—and only where they are indisputably welcome. The headquarters of the 5th Fleet would remain in Bahrain, for example, but fewer American warships would ply the waters of the Gulf. The air force would retain its huge new base in Qatar. The army might keep some prepositioned equipment in Kuwait and Qatar, regularly rotating in battalions to train on it. And if a future Iraqi government were amenable, the United States might retain an air base and some ground presence there. Otherwise, army bases in the region might be dispensed with altogether, and the United States could simply rely on equipment stored on container ships stationed at Diego Garcia, in the Indian Ocean.

are unnecessary. A reduced U.S. military and political presence would also weaken Washington’s ability to press its local allies to make the tough choices necessary for their own long-term well-being.

A return to an over-the-horizon posture would also risk recreating some of the problems that made the strategy untenable years ago. If Iran were to acquire nuclear weapons, a minimal U.S. presence in the region might tempt it to new aggression. The GCC countries have often been willing to accommodate powerful, aggressive neighbors and might again—giving Iran, say, an unhealthy control over oil flows. And a U.S. pullback might tempt other outside powers, such as China, to fish in the Gulf’s troubled waters.

tional rearmament while obviating its need to acquire WMD to deter Iran. As a bonus, if Persian Gulf publics could be convinced that American forces were there as part of a community of equals, an alliance might also help legitimize the U.S. presence.

This approach too has drawbacks. Most seriously, leaders of the GCC states do not want a formal alliance with the United States, at least not now. They fear that it would be seen as the ultimate act of colonialism and cronyism and would delegitimize their own regimes. A pro-American Iraqi government might feel the same unease. Nor would an alliance address the threat of domestic instability. If Tehran, with its weak military, decides to become more aggressive, it would more likely try to

undermine its neighbors from within than attack them directly. And a Persian Gulf alliance, despite its fearsome punching power, would still be vulnerable to an enemy that hits below the belt.

A Gulf Security Condominium

A third course—a security condominium modeled on arms control in Europe at the end of the cold war—offers the tantalizing prospect of handling both external aggression and internal instability.

Beginning in the 1970s, NATO and the Warsaw Pact engaged in a host of

down more easily in Baghdad. Likewise, if a regional security condominium could eventually defang Iran and lock in limits on Iraq, it would address GCC security problems without having to rely on a heavy, destabilizing American military presence. Moreover, a region-wide forum might make U.S.-GCC military relations more palatable to the people of the Gulf.

The forum might even be acceptable to Iran. For 20 years, Tehran has demanded that the United States, Iraq, and the GCC take seriously its security concerns. Offering a venue in which to discuss those concerns could give

security condominium work. In Europe it took 20–25 years of excruciating negotiations. Putting all the pieces together in the Persian Gulf would be harder. All the parties would come to the table with their own agendas and would try to subvert or structure the process to address only their own issues. A host of often hidden intra-GCC insecurities would come to the fore. The Iranians might demand Israel's inclusion, a call that would have tremendous resonance among the Gulf's Arab populations but that could scuttle the process by saddling it with the endless disputes of the Arab-Israeli peace process.

If it could be made to work, a security condominium would offer the best prospect of stabilizing and securing the region.

security engagement forums, confidence-building measures, and arms control agreements, such as the Commission on Security and Cooperation in Europe and the Mutual and Balanced Force Reductions talks, to address all the continent's security issues as a whole. Negotiating these deals took more than two decades but, in the end, produced a much more stable and secure Europe.

In the Persian Gulf, a security condominium would bring together the United States, the GCC countries, Iraq, and Iran. The parties would first establish a regional security forum in which to debate relevant issues, exchange information, and frame agreements. They could move on to confidence-building measures, such as notification of exercises and exchanges of observers, and ultimately to arms control, including demilitarized zones, bans on destabilizing weapons systems, and balanced force reductions for all. They might aim for a ban on all WMD, with penalties for violators and multi-lateral (or international) inspections to enforce compliance.

Such an approach has much to recommend it. It would be the least ram-orous way to handle the inevitable prohibition on Iraqi WMD. If all the regional states were working toward similar disarmament and Iraq was simply the one leading off, the pill would go

Tehran the sense that it was finally getting the respect it thinks it deserves. More to the point, it is the only way for Iran to affect U.S. military forces. Such a system could work only if Washington were willing, as it was in Europe, to limit its regional deployments. That by itself might be worth the price of admission for Iran.

If Tehran's hard-liners opted not to participate, they would isolate themselves both internally and internationally. At home, they would be hard-pressed to justify any action based on a supposed threat from the United States (or Iraq or the GCC) if they were unwilling to address that threat through diplomacy and arms control. To foreign audiences, Tehran's refusal to accept a U.S. olive branch would seal its identity as a pariah state with no interest in addressing its security concerns peacefully—thus making it easier for Washington to muster international support for tighter sanctions and other forms of pressure if necessary.

Some might fear that a security condominium would legitimize Iran's current government. But, as experience in Russia and Eastern Europe suggests, a security condominium would not stand in the way of regime change if that was where political development was heading.

The real problem would be making a

If it could be made to work, a security condominium would offer the best prospect of stabilizing and securing the region. The United States should publicly embrace it as its ultimate goal and start moving in that direction promptly. Convening a conference on Persian Gulf security toward that end could help legitimize the U.S. presence in the region and discredit those who oppose it.

But because a security condominium would be the work of years if not decades, it should not become the sole focus of U.S. efforts to create a new security architecture in the region. In an ongoing process Washington might use all three approaches. It could move quickly to diminish force levels. Meanwhile, it could begin exploring the possibility of a new alliance system or a process to construct a security condominium. The prospect of a new U.S.-GCC-Iraqi alliance might push Iran to participate in a security condominium, while the prospect of a security condominium might make an alliance more acceptable to GCC states. Ultimately, if the security condominium succeeded, peace were maintained, and forces throughout the region were considerably reduced, the way might be clear for a truly over-the-horizon American presence in the Persian Gulf—a development that would be greatly welcomed by all. ■

THE SIBERIAN CURSE

Does
Russia's
Geography
Doom
Its Chances
for Market
Reform?

By Fiona Hill and Clifford Gaddy

Siberia, like “the cold,” has for centuries been synonymous with the very image of Russia. From the tsars, who first planted the seeds of cities in Siberia, to the Soviet central planners, who moved masses of people and industry into its vast and remote regions, the exploration and development of Siberia have shaped Russia's sense of national identity. Siberia's “untamed frontier” has long promised wealth and opportunity for the rest of Russia.

Seventy years of Soviet rule, however, transformed that promise into something more akin to a curse.

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Even though central planning has been abolished, its legacy remains—an almost unimaginably poor distribution of labor and capital that can neither be easily maintained nor adapted to the market. Today, thanks to Soviet economic policies, Russia has a severely distorted economic geography. In particular, a huge portion of modern Russia—cities, factories, and people—is lost in the distance and cold of Siberia. Until Russia's leaders come to terms with Siberia's misdevelopment—and overdevelopment—during the 20th century, their efforts to build a competitive market economy and a normal democratic society are likely to fail.

The Bolshevik Legacy

Over the course of five centuries the tsars made Russia the world's largest country. They created a state defined by its physical geography, with a national identity rooted in territorial expansion, culminating in the conquest of Siberia. But it was the Soviets who shaped modern Russia's economic geography. Where the tsars had placed forts, villages, and towns in Siberia, Soviet rulers deployed millions of labor camp inmates to build giant power stations, factories, mines, and railways, as well as cities. The tsars bequeathed to the Bolsheviks a huge swathe of the world's coldest territory, but the Bolsheviks chose to defy the forces of both nature and the market in developing it.

Only the Soviet Union—a totalitarian control of production, and with

Thanks to Soviet industrialization and mass settlement of Siberia, much of Russia's population today is scattered over a vast land mass in large but isolated cities and towns. Inadequate road, rail, air, and other communication links hobble efforts to connect those population centers, promote interregional trade, and develop markets. About one in ten Russians live and work in almost impossibly cold Siberian cities, places where average January temperatures range from -15 to -45 degrees Celsius (+5 to -49 degrees Fahrenheit). Because of their location, these cities still depend heavily, as they did in the Soviet era, on central government subsidies for fuel, food, and transportation. Costs of living are as much as four times higher than elsewhere in the Russian Federation, while costs of industrial production are sometimes higher still.

Siberia and the GULAG

At the end of the tsarist period, the interior of Siberia was barely charted, let alone settled. The large-scale settlement and urbanization of Siberia were not possible under the tsars. The

How Cold?

How cold are Russia's cities? A comparison with Canada and the United States is instructive.

A list of the 100 coldest Russian and North American cities with populations of more than 100,000 would have 85 Russian, 10 Canadian, and 5 U.S. cities. The first Canadian city to appear on the list (Winnipeg) would be in 22nd place.

The coldest U.S. city (Fargo, North Dakota) would rank 58th.

Americans are accustomed to thinking of Alaska as the ultimate cold region. But Anchorage, Alaska, would not appear on a list of the coldest Russian and North American cities of more than 100,000 until position number 135, outranked by no fewer than 112 Russian cities. The explanation for this result is not that Alaska isn't cold. It is. It's just that Americans don't build large cities there. (In fact, Anchorage is the only city in Alaska with a population greater than 100,000.)

For really large cities, things are even more skewed. The United States has only one metropolitan area—Minneapolis-St. Paul—with more than half a million people that has a mean January temperature colder than -8° Celsius (18° Fahrenheit). Russia has 30 cities that big and that cold.

The GULAG and its virtually inexhaustible pool of slave labor became fundamental tools in the industrialization of Siberia. GULAG inmates—some 18 million–20 million of them over slightly more than two decades—facilitated the exploitation of timber and mineral resources in unpeopled remote areas. They also laid railroads, constructed roads and dams, dug canals, developed oil fields, and built factories and farms, all under monstrously inhuman conditions.

World War II gave further impetus to Siberian development when key factories were moved from European Russia eastward into the Ural Mountains and beyond, to put them out of the reach of invading German forces. Siberia received 322 relocated plants. Postwar economic development plans encompassing both these and yet-to-be-built industrial facilities demanded even more forced labor. Continuously, from mid-1949 until Stalin's death in 1953, the forced labor camps contained around 2.5 million inmates, half of whom had committed crimes no more serious than theft. During those peak years in the late 1940s and early 1950s, the GULAG accounted for an estimated 15–18 percent of all Russian industrial output and industrial employment.

Siberia after Stalin

The GULAG was largely dismantled after Stalin's death, but it had already laid the basis for what was to become a massive project of Siberian development under his successors. Many motives converged in the postwar development of Siberia. Communist economic planners sought to extract Siberia's oil, gas, diamonds, gold, and other rich mineral deposits to make the Soviet Union self-sufficient in strategic resources. Military planners, who during the war had already begun to reconcep-

ian state with coercion at its core, with its highly centralized absolutely no sense of cost—could conquer Siberia.

costs of peopling, exploiting, and maintaining such a vast, cold area were simply too onerous for their market-oriented economy. Only the Soviet Union—a totalitarian state with coercion at its core, with its highly centralized control of production and redistribution of resources, and with absolutely no sense of cost—could conquer Siberia.

Like the tsars, the Soviet state used Siberia both as resource frontier and as penal colony. But the Soviets developed the tsars' Siberian penal system to levels previously unimagined. Under Josef Stalin, the government launched the labor camp system in 1929 for the explicit purpose of colonizing and exploiting the natural resources of the nation's most remote regions. By 1934, half a million Soviet citizens—everyone who had received a prison sentence of three years or longer—were in the GULAG (an acronym based on the name of the department within the Soviet police ministry that ran the camp system). Stalin's great purges of the late 1930s brought the total camp population to more than 2 million.

tualize Siberia as a strategic redoubt—a defensible core deep in the interior—wanted to ensure that the entire region would be settled and secured. Soviet politicians tasked with engineering and mobilizing society in the 1960s–80s stressed the ideology of “conquering new lands”—now to be interpreted as campaigns to overcome nature and the wilderness through industrialization—to increase the strength of the Soviet state.

Planned “Cities”

Cities were an important feature of the plans for a Siberian industrial utopia. Cities were developed in Siberia in tandem with industries to provide a fixed reserve of labor for factories, mines, and oil and gas fields. In many respects, however, the cities were not really cities. Rather than being genuine social and economic entities, they were physical collection points, repositories, and supply centers—utilitarian in the extreme. They were built to suit the needs of industry and the state, rather than the needs of people. Indeed, primary responsibility for planning and constructing city infrastructure fell to the

Soviet economic ministry in charge of the enterprise the city was designed to serve. Few responsibilities were assigned to the municipal governments.

Still the cities grew, in both number and size. By the 1970s the Soviet Union had urbanized its coldest regions to an extent far beyond that of any other country in the world. (See box on page 25.) At precisely the time when people in North America and western Europe were moving to warmer regions of their countries, the Soviets were moving in the opposite direction.

Boom...and Bust

In the 1970s and early 1980s, Siberia and the Russian Far East dominated Soviet regional development programs. Western Siberia, rich not only in oil but also in natural gas, was on its way to becoming the largest energy-producing region in the USSR, and grand long-term industrial projects were being planned for the whole of Siberia. Western analysts were astounded by the magnitude of the projects and by the scale of investment necessary to carry them out.

But the Soviet economic slowdown of the late 1970s would put an end to such ambitions. By the 1980s the massive investments in Siberia and the Far East were offering extremely low returns. Many huge construction projects were left incomplete or postponed indefinitely. At first, the troubles were blamed on disproportional and incoherent planning, ineffective management, and poor coordination. But by the reformist era of the late 1980s under Mikhail Gorbachev, the problem was seen to be Siberia itself as well as the efforts to develop it. Criticism of the giant outlays in Siberia became commonplace. Regional analysts and planners in Siberia mounted a fierce rearguard action. They tried to justify continued high investment by pointing to the value of the commodities produced in Siberia on world markets and the state's dependence on Siberian natural resources and energy supplies. Still, by 1989 the industrialization of Siberia was beginning to seem a monumental mistake. The Siberian enterprise was, in any case, brought to a screeching halt by the collapse of the Soviet Union in 1991 and the beginning of Russia's macro-economic reforms in the 1990s.

Shrinking Russia

For more than 50 years, Soviet planners built Siberian towns, industrial enterprises, and power stations—although often not roads—where they should never have been built. Huge cities and industrial enterprises, widely spread and for the most part isolated, now dot the vast region. Not a single Siberian city can be considered economically self-sufficient. And pumping large subsidies into Siberia deprives the rest of Russia of the chance for economic growth.

To become competitive economically and to achieve sustainable growth, Russia must modernize and connect its physically vast but misdeveloped economy. But real change and modernization cannot be pursued within the framework of Russia's current economic geography. Refurbishing and upgrading the existing systems of road, rail, and air transporta-

tion, for example, or adding new infrastructure and new means of communications would simply improve the connections between towns, cities, and enterprises that should never have been where they are. It would make places more livable where, from an economic point of view, most people should not live to begin with.

Rather than try to "fix" its misdeveloped economy through further investment in Siberia, what Russia needs to do is the opposite. It needs to focus its attention on redeveloping the regions that are potentially most productive, those in the western part of the country. A large part of Siberia's current population needs to move to those areas, which are both warmer and closer to the markets of Europe. In effect, this is a policy to "shrink" Russia—but one that does so by concentrating its economic geography, rather than by divesting territory.

At precisely the time when people in the coldest regions of their countries, the So-

A New Approach to People

Not only does such a strategy of shrinkage run counter to Russia's imperial and Soviet history of territorial expansion, it also would require abandoning the centuries-old policy of constraining and directing the movement of the Russian people. To shrink Russia's economic geography in a sensible way, the government must set as one of its highest priorities facilitating the free movement of people within the Russian Federation. Even today, although the legal right to move is enshrined in the constitution, Russians are still not free to relocate wherever they would like to live and work. Residence restrictions in cities like Moscow, together with resource constraints, poorly developed job and housing markets, and the absence of social safety nets, obstruct personal mobility. The government needs to remove such overt and hidden barriers so that people can move where they want.

While many Russians will welcome the opportunity to move, for others the downsizing of Siberia will be painful. Many people who would like to move are too poor to do so, and the worse the economic situation becomes in the region, the less they are able to move. The Russian Federation is not rich enough to finance a mass relocation, and today few places in Russia can offer new jobs. To the extent that it can, however, the government should help move people, especially younger and more productive people, out of Siberia to European Russia. It should offer housing relocation packages or lump-sum payments or bonuses to help them move. It could, for instance, finance migration through a special fund generated by revenues from Siberian natural resource wealth.

The biggest challenge will be dealing with the many residents of Siberia who are too old or too unskilled to find jobs elsewhere. Their assets in the region are worthless and cannot be sold to finance their relocation. For these people, the Russ-

ian central and regional governments will have to continue fuel, food, and other subsidies in the coming decades to make life bearable. But the subsidies must be transparent so that the population elsewhere in Russia, as well as in Siberia, knows who is paying for what and why.

Realistic Strategies for Siberian Development

British geographer Michael Bradshaw has recommended that Russia adopt a “cleaner, leaner approach” to the development of Siberia and the Far East—shifting from labor-intensive methods to labor-saving technologies and industries that can easily shed labor or employ temporary workers. This is exactly the right approach, even if it means renewed emphasis on the region’s extractive and energy industries. They are the only sectors that can rely on (and pay the high wages to attract) outside workers on short-term tours of duty.

Moving Ahead

Market mechanisms alone will not solve the problems that stem from Russia’s distorted economic geography. To reconcentrate its population in the west and correct the misallocations in its economy, Russia will need active, even bold, state policies. Even so, those policies will have to be modest in their expectations. The Stalinist process that put people in Siberia in the first place cannot be reversed wholesale. People will not move en masse, and the goal is not, in any case, to “empty out” this resource-rich region, but to help it move closer to the kinds of economic activity, and thus the population, that might have been expected under market conditions.

One big obstacle to effecting change will be the governors, oligarchs, and others based in Siberia who have vested interests in continued regional subsidies and redevelopment programs. President Putin and other national leaders will have to place

North America and western Europe were moving to warmer climates while Russia and Siberia were moving in the opposite direction—into the cold.

Canada offers an appropriate model. Canada’s North is a resource base, but the bulk of the nation’s people are located along the U.S. border, close to markets and in the warmest areas of the country. According to the 2002 Canadian Census, Canada’s northern territories have less than 1 percent of the nation’s total population. Canada’s mining industry—and northern industry in general—relies on seasonal labor, with the labor pool shrinking during the coldest winter months and increasing again in summer.

Were Russia to adopt a similar approach, most of its population would live closer to the markets of Europe, also in the warmer areas of the country. Siberian cities would be much smaller than at present. In very remote areas where key natural resources are located, settlements would be outposts (not towns and cities), with small permanent populations and a heavy dependency on seasonal workers for the bulk of production in the summer months.

New Conceptions of Security

Finally, Russia will have to rethink security issues as it contemplates the prospect of “empty lands” in Siberia and the Russian Far East. Despite popular Russian fears, most serious analysts do not foresee a mass influx of migrants from China across Russia’s borders. Still, given that Russia borders countries that may not always remain friendly, its security concerns do need to be addressed. Enhanced technical systems—for instance, the creation of sensors, new rapid reaction forces, and high-tech weapons—could replace the deployment and support of large conventional land and sea forces on Far East borders. More important in the long term would be cooperative solutions such as an international treaty with neighbors like China and the United States to guarantee Russia’s territorial integrity and its continued sovereignty over Siberia and the Far East.

themselves above such regional interests. They should send out clear signals that the future of Russia (and, consequently, also of Siberia) depends on a strong, integrated, and connected Russia, which will not be achieved if the government continually pumps resources—not least, human resources—out of more productive areas and into Siberia.

Russia needs to achieve, as best it can, a match between its most productive (or potentially most productive) regions and its most productive capital, including people. That involves putting Siberia in its proper context—which means, in at least one respect, reviving the ancient myth of Siberia’s promise. The wealth of Siberia is not Siberia’s. It is Russia’s. It so happens that much of Russia’s wealth—and the bulk of its natural resources—are located in Siberia. But Siberia cannot claim these as its own, as much as the oligarchs and local government officials there may want to.

Russian leaders do not face a choice of developing Siberia or rejecting it and casting it off. As they make it possible for most of Siberia’s people to move elsewhere, they can develop the region’s resources realistically—reducing its dependency on huge fixed pools of labor and shifting to more technologically intensive methods of extraction and temporary work schemes.

Today, Siberia’s resources are being developed at far too high a price. Enterprises outside the energy sector cannot generate sufficient revenues to pay high wages to attract new labor or to keep the existing labor force. Instead, administrative, nonmarket mechanisms keep people in place—heavily subsidized to the detriment of Russia as a whole. Siberia’s resources can contribute to Russia’s future prosperity, and the regional economy can one day be viable, but not if the Russian government persists in trying to maintain the cities and industries that communist planners left for it out in the cold. ■

THE BATTLE

By Thomas E. Mann

OVER CAMPAIGN FINANCE

Prospects for the New Reform Law

America's reputation as the very model of a vibrant constitutional democracy has been tarnished of late by low voter turnout, uncompetitive elections, shoddy administration of elections, and the politicization of electoral rules. Making matters even worse have been recent campaign finance practices. Fundraising abuses in the Clinton White House ushered in an era of blatant disregard for federal campaign finance law. Longstanding prohibitions on corporate and union treasury financing of federal election activity were rendered obsolete. Elected and party officials avidly solicited "soft-money" contributions from sources and in amounts proscribed by federal law. And parties and interest groups discovered that they could use "issue ads" to influence federal elections, thereby escaping the disclosure requirements and contribution limits that govern election campaigns. By the 2000 election, parties and groups geared their fundraising efforts and campaign strategies to take full advantage of these loopholes in federal law.

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ILLUSTRATION BY VICTOR JUHASZ

The Bipartisan Campaign Reform Act, signed into law by President Bush on March 27, 2002, attempts to halt these abuses of current law. Whether the new law will be effective, however, will be critically shaped by the Supreme Court's promised ruling on the constitutionality of its various provisions and by administrative rulings and enforcement actions by the Federal Election Commission. The efficacy of reform will also depend on the responses by political actors to the regulatory regime that emerges from these judicial and administrative actions.

The Reform Law and What It Does

The seven-year struggle to enact the Bipartisan Campaign Reform Act of 2002 was an extraordinary legislative odyssey. Overcoming the self-interest of incumbents, philosophical differences, partisan calculations, interest group opposition, low public salience, presidential indifference, constitutional limitations, and the inherent difficulty of regulating money in politics was a daunting challenge. Critical to eventual enactment were the tenacity of the chief congressional sponsors, the steadfast support of a small group of moderate Republicans, a decision by proponents to pursue a scaled-down reform agenda, the availability of new research that helped define specific regulatory approaches, Senator John McCain's emphasis on reform during his quest for the Republican presidential nomination in 2000, Democratic gains in the Senate later that year, the surprising and consequential efforts by Democratic leaders Tom Daschle and Richard Gephardt to pass the legislation, and an unusual level of pragmatism within a reform community that had long since lost any illusions about what it was going to achieve. Ultimately, support for a filibuster against the bill in the Senate eroded to the point at which majority will prevailed and the bill was finally adopted.

The act bans the raising of soft money (funds subject only to state, not federal, restrictions) by national parties and federal officeholders and candidates. It restricts soft-money spending by state and local parties on what are defined as "federal election activities." It also brings

under regulation for the first time a class of issue advocacy broadcast ads, labeled "electioneering communications." Although other issue advocacy ads remain unregulated, those that pass a three-point "bright-line test"—do the ads refer to a clearly identified candidate for federal office? are they targeted on the constituency of that candidate? are they broadcast within 30 days of a primary or 60 days of a general election?—must be financed and disclosed consistent with existing federal law. Corporations and unions are prohibited from spending treasury funds, directly or indirectly, for such electioneering communications. The reform act treats electioneering communications that are coordinated with a candidate or party as contributions to and expenditures by a candidate or party. It also increases the amount of "hard money" (funds subject to federal regulation) that individuals can contribute to candidates and parties, while raising limits on individual and party support of any candidate whose opponent exceeds certain levels of personal campaign spending (known as the Millionaires' Amendment).

The Court Challenges

Proponents of the new law view it as a long-overdue package of reforms designed to restore the system of campaign finance envisioned by Congress when it adopted and amended the Federal Election Campaign Act in the 1970s. Its purpose, they argue, is to block the loopholes that increasingly allow violation of longstanding prohibitions on corporate and union treasury financing of federal elections and disclosure requirements for federal electioneering.



Proponents of the new law view it as a package of reforms to restore the system of campaign finance envisioned by Congress when it adopted and amended the Federal Election Campaign Act in the 1970s.

Opponents see the law as much more ambitious and ominous—a wholesale assault on protected First Amendment speech and rights of political association. They argue that the law's restrictions would unconstitutionally limit the rights of individuals and groups to participate in federal elections and the abil-

ity of national, state, and local parties to work cooperatively to promote candidates and issues at all levels of the political process.

Given these widely divergent views of the new law, it was no surprise when a highly diverse set of individuals and groups (spanning the political spectrum from the Republican National Committee to the California Democratic party and ranging in political ideology from the National Rifle Association and various right-to-life groups to the AFL-CIO and American Civil Liberties Union) rushed to court to challenge the law as soon as it was signed. The law was

defended by the Department of Justice, the Federal Election Commission, and the act's principal congressional sponsors, who were accorded status as "intervenor-defendants" in the litigation, with the same legal prerogatives as the named defendants.

Anticipating such litigation, Congress had made provision in the law for expedited judicial review of any constitutional challenges, beginning with a trial before a three-judge panel in the federal district court of the District of Columbia and then allowing a direct appeal to the Supreme Court. The trial court consolidated all the separate complaints brought by plaintiffs into a single case, *McConnell v. FEC*, and decided to dispense with live testimony and cross-examination in court and instead rely

on a paper trial. As a consequence, plaintiffs and defendants assembled a voluminous body of evidence and argumentation—many thousands of pages of fact and expert reports, depositions, cross-examinations, documents, and legal briefs.

The trial court panel, after a December 2002 hearing, was widely expected to issue its opinion by the end of January. Instead, it struggled—for the most part unsuccessfully—for months to reach consensus on findings of fact and conclusions of law. Finally, on May 1, the panel disgorged more than 1,600 pages of opinions and orders, featuring a limited *per curiam* opinion signed by two judges and lengthy separate opinions by all three. The opinions revealed a fractious and personally contentious panel, one able to present the Supreme Court with neither an agreed-on summary of the facts of the case nor a clear and consistent exposition of the constitutional issues.

The panel upheld parts of the two pillars of the act—the soft-money ban and the regulation of electioneering communications—but ruled other parts unconstitutional. Two judges accepted the characterization of recent campaign finance practice presented by the defendants, namely, in Judge Richard Leon's words, "the use of corporate and union treasury funds, either directly or through soft money donations to political parties, to finance electioneering communications masquerading, predominantly, as issue ads." They also agreed that the defendants had demonstrated the constitutionally necessary case for Congress to remedy this problem. Disagreeing on the basis for judging whether specific remedies are legitimate, however, they labored to produce what both probably regard as sub-optimal compromises. The third member of the panel, Judge Karen Henderson, largely took herself out of the panel's opinion by characterizing the entire statute as a wholesale assault on the First Amendment. Surprisingly, the one exception was her conclusion that the prohibition on soft-money fundraising by federal officeholders is constitutional.

Had this fractured opinion been allowed to stand until the Supreme

Court issued its decision, the 2004 election cycle would have been shrouded in legal uncertainty. But the district court panel's decision was stayed, and the Supreme Court announced an expedited briefing schedule over the summer and a hearing on September 8, a month before the formal start to its fall term. The decision is expected by December, just before the official kickoff of the presidential nominating process.

It is extremely difficult to calculate how, if at all, the work of the three-judge panel will influence the Supreme Court. The district court panel's limited findings of fact and idiosyncratic conclusions of law suggest the justices may well begin from scratch. In fact, by directing the plaintiffs to submit the initial brief on the full range of their challenges to the new law, the Court has signaled that it is likely to consider the case *de novo* and not have its agenda set by the district court opinion. There is no way of knowing whether the Court will give special weight to the fact that a conservative member of the district court panel, Judge Leon, found an adequate basis for Congress to regulate party soft money and issue advocacy. It seems unlikely that a majority of justices will facially dismiss the reform act in the fashion of Judge Henderson. The critical question is whether they will find compelling the rationale used by Congress to prevent circumvention of federal election law and uphold provisions of the reform law that Judge Leon could not.

The Research Wars

A fascinating dimension of this legal battle is the public campaign to support or discredit the evidence used by the contending parties to buttress their legal arguments. Joseph Sandler and Robert Bauer, prominent Democratic election law lawyers who serve as counsel to the Democratic National Committee and the House and Senate Democratic campaign committees, are among the most outspoken critics of the new law, which passed with the nearly unanimous support of congressional Democrats. Like their Republican counterparts, Sandler and Bauer argue that the new law tram-

ples on the speech and associational rights of political parties and improperly extends the reach of federal law into nonfederal election activities.

These arguments are part of a disagreement over whether the rise of party soft money and issue advocacy has strengthened or weakened political parties. The dispute centers on such questions as whether state parties are independent actors and genuine partners or mere instruments and funding conduits of national parties and federal officeholders; how much soft money has been used for party-building and grassroots activities and how much for broadcast advertising on behalf of specific federal candidates; and whether parties dilute the influence of large donors or facilitate their access to policymakers.

Answers to these questions, in turn, shape assessments of the provisions of the reform act directly affecting party finance and forecasts of how parties will fare in this new regulatory environment. Will national party committees be able to compensate for the abolition of soft money by raising substantially more hard money? Will the new restrictions on state parties dealing with federal election activities constrain their efforts on behalf of state and local candidates? Will parties be put at a disadvantage in comparison with interest groups? Will large soft-money donors (corporations, unions, and individuals) find indirect and less accountable ways of financing federal campaign activities? These questions will ultimately determine the practical impact of the ban on party soft money. They are also shaping the public debate surrounding the litigation that will decide the provision's constitutionality.

A spirited public debate has also enveloped the new law's treatment of issue ads and electioneering communications. One element of this debate centers on a legal disagreement. When the Supreme Court in *Buckley v. Valeo* (1976) limited disclosure requirements and prohibitions on corporate and union funding of independent expenditures to communications that "expressly advocate the election or defeat of a candidate for federal office," did it leave any constitutional space for

Congress to define and regulate a category of electioneering communications separate from express advocacy? If not, Congress would be unable to regulate an increasingly important class of campaign activities designed to influence federal elections.

Supporters of the reform act have rested much of their case for regulating electioneering communications—and for the specific bright-line test to define such communications—on a body of new research on television ads sponsored by candidates, parties, and groups. Opponents have challenged the methodological underpinnings of the research, going so far as to accuse analysts at the Brennan Center for Justice, at the New York University School of Law, of manipulating the data to produce the desired results. Conservative columnists have railed against “the debasement of scholarship for partisan purposes” and the deliberate faking of evidence underlying the constitutional justification of a key provision of the act.

Opponents of the new law, however, have not reanalyzed these studies (although the data are publicly available) or offered their own findings and conclusions based on alternative research. They have not even challenged many of the findings from this research, including the ever-increasing concentration, as election day approaches, of party and interest group “issue ads” mentioning or depicting a federal candidate in hotly contested races. Nor have they offered any counter to the scores of pages of testimony by politicians, party officials, political consultants, interest group leaders, and donors who corroborate the findings of the Brennan Center research.

One legitimate issue did arise in this

contretemps. How would the bright-line test for electioneering communications affect pure issue ads? According to a measure formulated by Jonathan Krasno, the share of pure issue ads that would be drawn into the net of regulation by the bright-line test was 6 percent in 1998, 3 percent in 2000. The Court will have available alternative measures and their rationales as well as a fully transparent data set with which to consider the possible impact of the new law. One hopes the justices will not be distracted by the public campaign to vilify the researchers.

What's Ahead?

Despite the uncertainty over which provisions of the act will be upheld or reversed by the Supreme Court, the law has already prompted a set of administrative rulings by the Federal Election Commission and strategic adjustments by various political actors. Some of the FEC's initial decisions have themselves been controversial, prompting legal challenges by individuals and groups supporting the new law. The next critical stages will materialize if and when the FEC adjusts and applies these rules in response to the Supreme Court's decision and as enforcement issues arise under the new law.

President Bush is widely viewed as a primary beneficiary of the new law. His decision to forgo public matching funds in the 2000 presidential nominating process freed him from expenditure limits and allowed him to outspend his Democratic opponent in the months before the party conventions. With the contribution limit raised from \$1,000 to \$2,000, Bush may well raise and spend \$200 million in 2004, compared with the roughly \$50 million that can be spent by candidates accepting public matching

funds. Unfortunately, the new law made no adjustments in the spending limits or matching formula for the presidential public finance system.

In the contests for the House and Senate, Democrats are also thought to be at a disadvantage, at least in the short term. In recent elections they have relied much more on soft money than have the Republicans. Initial fundraising reports in the 2004 cycle confirm that Republican party organizations retain a substantial hard-money fundraising advantage over their Democratic counterparts. But parties furnish a modest share of the funding in congressional elections, particularly under the new law's rules. They can no longer pump millions of dollars of soft money into issue ads in a handful of competitive races. They are likely to spread their resources more widely, invest additional funds in grassroots activity, steer funds raised by safe incumbents to competitive contests more aggressively, broker PAC contributions for key races, and mobilize voter identification and turnout activities of allied groups. Democrats need not be badly outclassed in this altered arena of competition.

The demise of soft money is not likely to diminish the importance of political parties. Parties are remarkably adaptive organizations absolutely essential to the functioning of democracy. Critical roles and ample resources remain for them in this new regulatory environment if they will seize the opportunity, as they almost surely will.

Even if the new campaign finance law survives the hurdles of constitutional challenge, administrative rulings, enforcement, and the strategic adaptation of political actors, substantial problems with money and politics remain. The new law was designed to plug the most glaring loopholes in federal election law. Now reformers must turn to other measures to enhance electoral competition, increase broadcast time available to candidates and parties, repair the presidential public finance system, and strengthen the enforcement process.

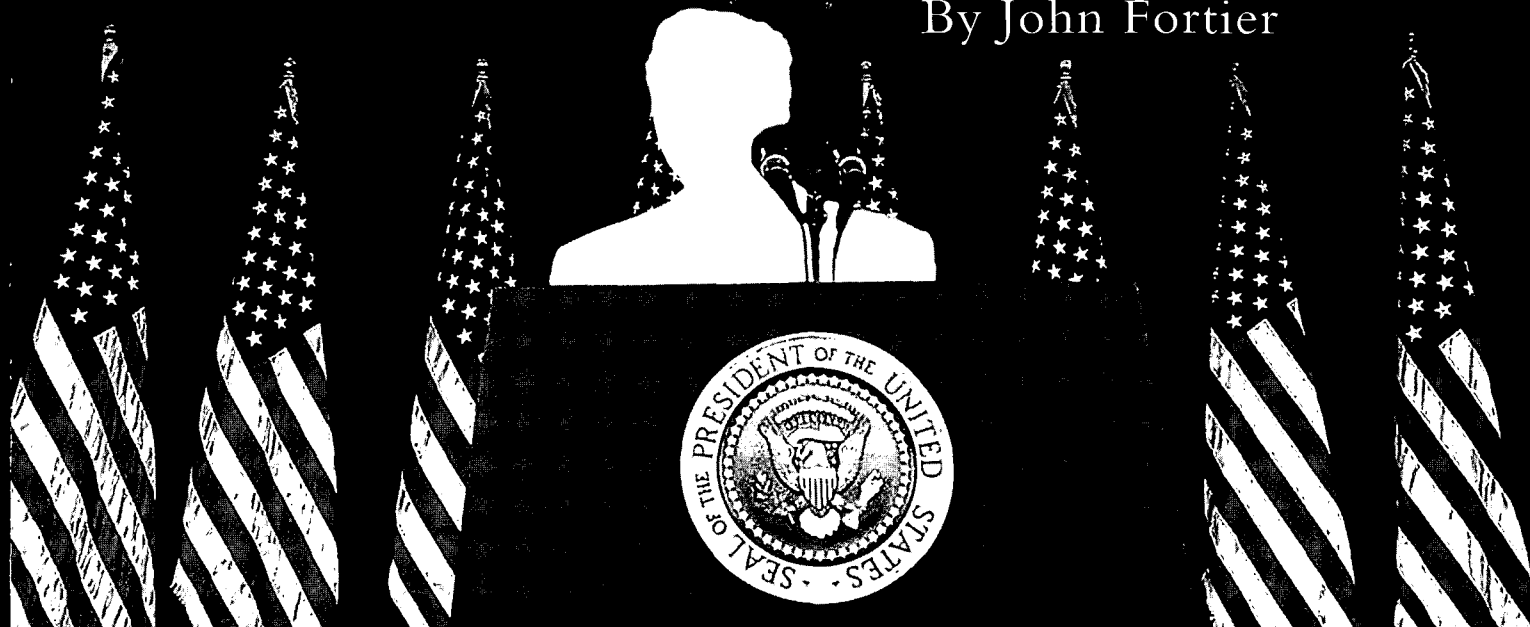
The realities of American politics still fall well short of our reputation as a democratic exemplar. ■

Opponents see the new reform law as much more ambitious and ominous—a wholesale assault on protected First Amendment speech and rights of political association.



PRESIDENT

By John Fortier



Michael Armacost?

The Continuity of Government after September 11

The phrase “President Michael Armacost” is a phrase with a familiar ring to it in the nation’s capital, for Armacost served ably as Brookings’ fifth president from 1995 to 2002. But Armacost might have become president not of Brookings, but of the United States. Had that happened, he would have needed all the leadership skills he had honed at the highest levels of the U.S. foreign service—and perhaps more. For an Armacost presidency would have come about because of a catastrophic terrorist attack, combined with potentially disabling quirks in the U.S. presidential succession system.

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The story begins on January 20, 1989, at the inauguration of the 41st president, George H. W. Bush. At noon on that day, President Ronald Reagan's term expired, and Chief Justice William Rehnquist administered the oath of office to Bush. What if, during that ceremony, terrorists had flown a plane into the West front of the Capitol, where the inauguration ceremony was taking place, or set off a powerful bomb? The result would have been chaos. Any attack against U.S. political leadership is a threat to national security, but the inauguration is the most vulnerable time for the government, when the mechanisms for providing an orderly transfer of power to a presidential successor threaten to break down.

President Bush and Vice President Dan Quayle were, of course, present at the ceremony. Next in line of succession were Speaker of the House Jim Wright and Senate President Pro Tempore Robert Byrd, both of whom attended the inauguration. A devastating terrorist attack would have killed all of them along with many members of Congress and several Supreme Court justices, including the chief justice.

So who would have been president? Next in line after the speaker and the president pro tem are the cabinet officers in the chronological order of the creation of their departments. But which cabinet? Because the attack came on Inauguration Day, George Bush had not yet nominated his cabinet. A several-hour interval always ensues between a new president's taking office at noon and Senate confirmation of the cabinet.

So in the case of a calamitous attack at an inauguration, the new president would have no cabinet, and the presidency would pass to the cabinet members of the previous administration. A presidential term has a beginning and end defined by the Constitution. At noon on January 20, 1989, the terms of President Reagan and Vice President Bush ended. But the terms of cabinet members are not constitutionally limited. Cabinet members stay in office until they resign, die, are impeached and convicted, or are removed by a president. So

The Continuity of Government Commission

The AEI/Brookings Continuity of Government Commission is co-chaired by Lloyd Cutler, an honorary Brookings trustee who served as White House counsel for Presidents Jimmy Carter and Bill Clinton, and former Republican Senator Alan Simpson. The commissioners include former House Speakers Thomas Foley and Newt Gingrich and two former White House chiefs of staff, Leon Panetta (Clinton) and Brookings trustee Ken Duberstein (Reagan). It also includes Judge Robert A. Katzmann, of the U.S. Court of Appeals for the Second Circuit, a former Brookings senior fellow. Others on the commission are Phillip Bobbitt, Charles Fried, Jamie Gorelick, Nicholas Katzenbach, Lynn Martin, Kweisi Mfume, Robert Michel, and Donna Shalala. The commission's first report, on the continuity of Congress, and its proceedings can be found in more detail at www.continuityofgovernment.org.

any of Reagan's cabinet members who had not resigned at noon would have remained in the line of succession. And in 1989, several additional wrinkles would have complicated still further the transfer of power from Reagan to Bush—highlighting yet again the difficulties in our presidential succession system. Three of Reagan's cabinet members—Treasury Secretary Nicholas Brady, Attorney General Richard Thornburgh, and Education Secretary Lauro Cavazos—stayed on after his term ended, as Bush had asked them to serve in his new administration. Reagan's other cabinet secretaries resigned at noon, leaving their departments in the hands of acting secretaries.

According to the Presidential Succession Act, an acting secretary of a department is in the line of succession as long as he or she has been confirmed by the Senate for some position. On January 20, 1989, at noon, Reagan's secretary of state, George Shulz, had resigned, as had the number-two person in the State Department, John Whitehead. The number-three person at State, the undersecretary for political affairs, who became acting secretary of state, was Michael Armacost. As the secretary of state is first among the cabinet in the line of succession, Armacost would have become president of the United States.

After the Bush inauguration the Senate did not move expeditiously to confirm President Bush's appointments to the cabinet. Typically, a president-elect makes his cabinet choices known to the Senate before the inauguration so that confirmation hearings can begin. Sometime after the inaugural ceremony, the new president submits formal nominations to the Senate, and the Senate comes in session late in the afternoon of the 20th to confirm the noncontroversial nominees. In 1989, with Republican George Bush replacing another Republican, Ronald Reagan, little sense of urgency attended the cabinet confirmations, as Republicans would occupy the offices before and after the switch. The Senate came in session on the afternoon of the 20th to accept the president's nominations to the cabinet, but almost immediately adjourned until Wednesday, January 25, when it returned to hold confirmation votes. That year Armacost sat four heartbeats away from the presidency for five days until the Senate confirmed James Baker to be the next secretary of state.

Planning for the Inconceivable

Before September 11, a scenario like that I've been describing would have seemed far-fetched in the extreme. But the shattering events of that day have made it essential to consider matters once deemed almost inconceivable. That is the mission of the Continuity of Government Commission, run jointly by Brookings and the American Enterprise Institute—to study how the three branches of government could survive a catastrophic attack.

The commission held hearings last fall on the continuity of Congress. Its first report this past June highlighted the problems of a catastrophic attack that left numerous vacancies in Congress, and it proposed a constitutional amendment to allow temporary appointments in catastrophic circumstances to fill vacant seats in the House until special elections could be held. The commission is now looking at the presidential succession.

The good news is that most changes to the line of presidential succession can be made by statute rather than by amending the Constitution. But ensuring the presidential succession requires addressing several troublesome issues. First, all figures in the current line of succession work and reside in the metropolitan Washington area. In the nightmare scenario of a nuclear attack, everyone in the line of succession could be killed. Second, many constitutional scholars doubt that it is constitutional for the speaker of the House and the president pro tempore of the Senate to be in the line of succession at all, because they do not meet the constitutional definition of "Officers" of the United States. Third, regardless of its constitutionality, some analysts question the wisdom of putting the president pro tempore of the Senate in the line of succession, because this largely honorific post is traditionally held by the longest-serving senator of the majority party. Fourth, some observers suggest that congressional leaders of the president's party should be in the line of succession; the current law allows for a switch in party control of the presidency if the speaker of the House or president pro tempore of the Senate belongs to a party different from the president's. Fifth, the line of succession proceeds through the cabinet members in order of the dates of creation of the departments they head. While several of the most important departments are also the oldest, it may not make sense to rely simply on historical accident. Instead, it may be necessary to evaluate the line of succession taking into account the present circumstances of the cabinet departments. For example, should the secretary of the interior be ahead of the secretaries of commerce, energy, or education? Sixth, if the line of succession passes to a cabinet member, the law allows for the House of Representatives to elect a new speaker (or the Senate a new president pro tempore), who could bump the cabinet member and assume the presidency at any time. Finally, the Twenty-fifth Amendment provides for several instances of presidential disability when the vice president can act as president, but it does not cover circumstances when the president is disabled and the vice presidency is vacant. In this case, the Presidential Succession Act allows congressional leaders and cabinet officers to act as president for a short time, but only if they resign their posts.

Who Succeeds President Armacost?

Now to return to the story. If terrorists had attacked on January 20, 1989, and Michael Armacost had become president, what would have happened next? One quirk in the Presidential Succession Act is that Congress is given a privileged position over the cabinet members, so subsequently elected congressional leaders might "bump" a cabinet member who had assumed the presidency. It is not an accident. The United States has had three succession acts. The first was in effect until 1886 and had just the two congressional leaders, but no cabinet members, in the line. A second law that governed succession from 1886 to 1947 removed Congress and had just cabinet members in the line of succession. The current act owes its creation to Harry Truman, who came to the presidency after a few months as vice president and after a career in Congress. He believed strongly that a successor to the president should be an elected figure. He pro-

posed, and Congress ultimately passed, a law that put congressional leaders back in the line of succession ahead of the cabinet. The law also specifies that if a cabinet member becomes president (meaning the president, vice president, speaker, and president pro tempore have perished), then once Congress elects a new speaker of the house or a new president pro tem, that congressional leader can "bump" the cabinet member and become president for the remainder of the term.

So an Armacost presidency would have lasted only until either the House or the Senate could have elected new leadership and one of those leaders could assume the presidency. But even this matter is not as straightforward as it might be. An inauguration ceremony is attended by most members of Congress. If a massive attack had hit the inauguration, many members would likely have been killed or incapacitated, and the House and Senate might well have had difficulty functioning. These problems of congressional continuity are addressed in detail in the commission's first report, but a brief account of the difficulties will show how the questions of continuity of the presidency and of Congress are intricately intertwined.

For both the Senate and the House a quorum requirement is laid out in the Constitution, with a majority of members of each body constituting a quorum. By a literal interpretation of the Constitution, if fewer than 51 senators or 218 House members are alive, neither chamber would have a quorum and so neither would be able to conduct any business. Because they could thus not elect new leadership, Armacost would remain president until they could. The problem of continuity is more acute in the House. In the Senate, vacancies can be filled almost immediately by governors who can make temporary appointments that last until a state can hold a special election. In the House, the only way to fill vacancies is by holding a special election, which takes on average four months. Yet another problem for both the House and the Senate is incapacitated members. If numerous members were incapacitated but alive, say in burn units or infected with a contagious biological agent, there would be no method to replace them, and the House and Senate might not function until enough members recovered.

But even the quorum requirement is not as simple as its constitutional language would suggest, for House parliamentary rulings over the years have come down in favor of a more lenient standard—for a quorum to be a majority of the "living" members. In that case, a small group of remaining members could elect a speaker. In an extreme case, five members of the House survive and by a vote of three to two elect a speaker. The new speaker would bump President Armacost and serve for the nearly four years remaining in the term.

All these scenarios are complicated and of course highly unlikely. Surely another president of Brookings would never assume the presidency of the United States from a subcabinet position? Perhaps. But on January 19, 2001, when Madeleine Albright resigned her post as secretary of state, the number-two person at State at the time was Strobe Talbott. As it happened, Talbott too resigned. Had he not, he would have become acting secretary of state, and our story could have begun again. ■

COPING WITH METHUSEL

The capacity to manipulate the genetic templates that shape all living beings was long the plaything of science fiction. In the final decades of the 20th century, however, intellectual advance transmuted genetic tinkering from alchemy into science. In 1953 two young scientists identified the double helix comprising four nucleotides entwined in the code of all life, thereby opening the first chapter in the saga of molecular biology. Then in 2001 two competing scientific teams produced a draft of the human genome, introducing a new therapeutic era in which medical professionals may be able to slow human aging and make celebrating 100th birthdays almost routine.

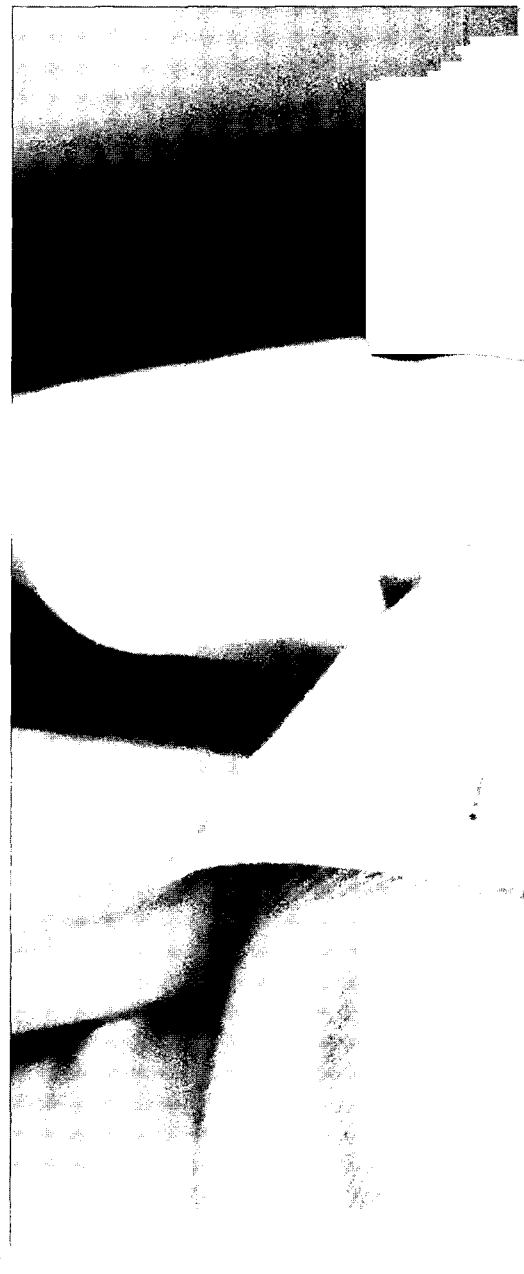
No one can predict the precise extent or timing of advances in molecular biology. No one can know exactly when particular diseases will be prevented or cured. No one can foresee when, or even if, human aging will be slowed or stopped. No one yet knows for sure whether humans' genetic makeup limits life span or, if it does, what those limits might be. Some families include more nonagenarians and centenarians than any roll of nature's dice could explain, a fact that suggests genes' powerful influence on longevity. Even if life span is now limited, molecu-

lar biology may reveal that these limits are not fixed and may provide ways to slow aging and prevent or cure illnesses that cause physical decline and death.

Scientific advance has revolutionized man's centuries-old assault on human illness. Physicians have long understood, in some sense, the basis of successful medical treatments, without being able to penetrate the underlying processes by which their interventions worked. The fundamental reasons why antibiotics killed pathogens, for example, remained for years as mysterious to the discoverers of those drugs and to the physicians who used them as they were to the patients whose lives they saved.

As the 21st century begins, scientists are increasingly working from a fundamental understanding of cells, proteins, and genes to design interventions that reverse, block, or otherwise forestall illnesses. In the words of Nobel Prize winner Alfred Gilman, scientists are now "able to complete [their] understanding of the wiring diagram of the signaling switchboard in each type of cell." With that knowledge in hand, they now have—or soon will—the means to design drugs or to directly change how cells operate to correct the genetic defects each person inherits or acquires during life from mutations or other sources.

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NORBERT SCHAEFER/CORBIS

In the coming century, human mortality rates may begin falling rapidly. Eventually molecular biology may lengthen human life almost unimaginably. Is the Age of Methuselah at hand? And if so, what will it mean for public policy in the United States—and the world?

AH

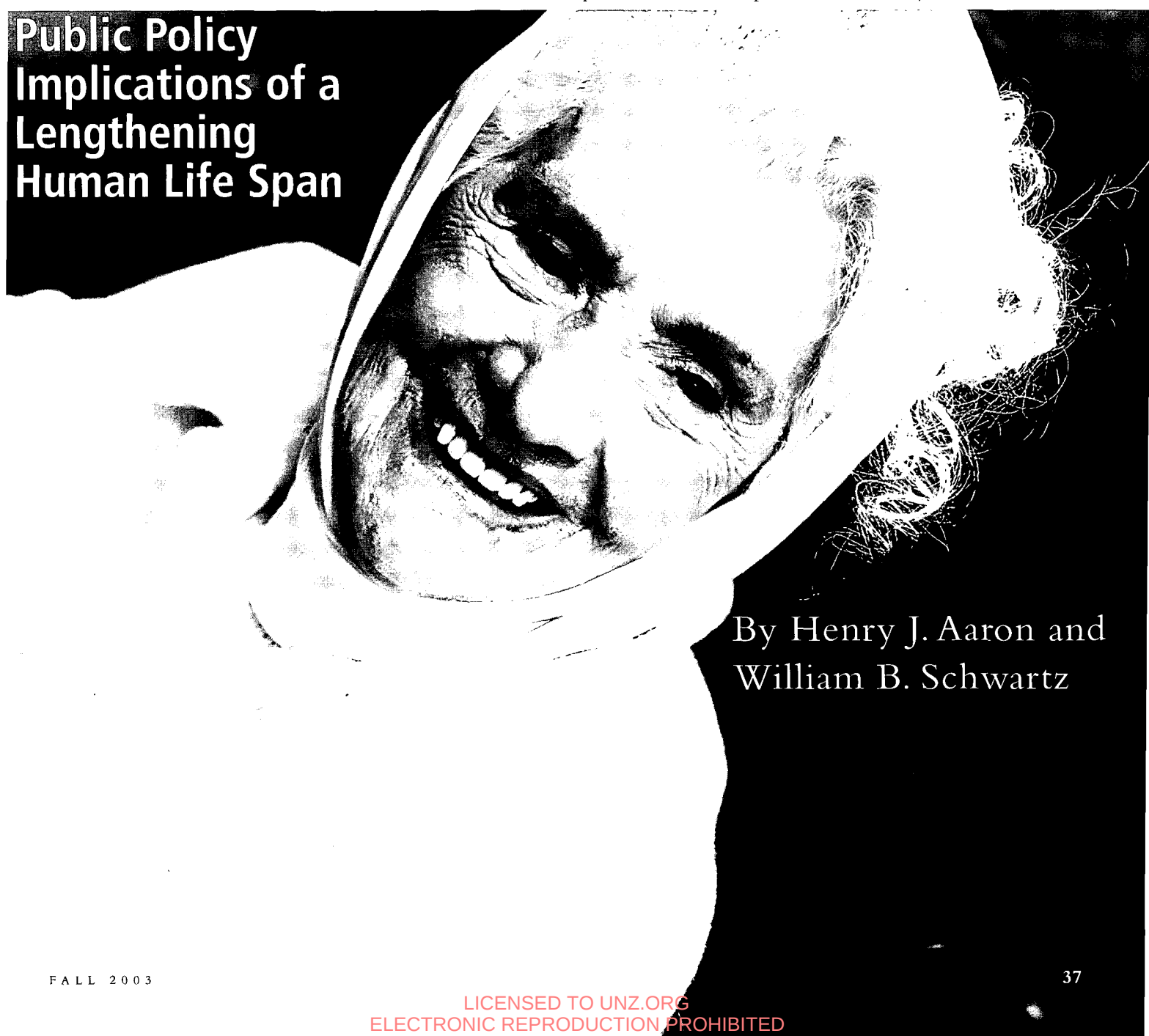
Our Uncertain Demographic Future

Advances in public health, nutrition, and medical treatment over the past century first set in motion an increase in human life expectancy. With mortality rates now declining roughly 0.6 percent a year, demographers project that longevity will continue to increase and that the elderly will constitute a growing share of the U.S. population. A biomedical revolution causing mortality rates to fall more rapidly could intensify these trends and have important demographic implications.

Many scientists have long believed that the human life span has a natural

limit. The finding by 19th-century scientist August Wiseman that cells stopped reproducing after a certain number of divisions seems consistent with this hypothesis. But even if a natural limit exists, the practical question is how far that limit exceeds current average life span and what can be done to push today's life span closer to that limit. One theory of aging draws an analogy between a person and a machine consisting of many systems, each essential for its operation. Each system within the machine remains functional until too many of its constituent parts fail, leading the machine itself to fail over time in patterns that closely resemble human

Public Policy Implications of a Lengthening Human Life Span



By Henry J. Aaron and
William B. Schwartz

mortality rates. The implication is that medical progress comes through interventions that prevent or postpone the failure of the constituent parts of each of the biological “systems” essential for life.

Rapidly falling mortality rates would affect longevity relatively quickly but would take many years to alter the age distribution of the population. The U.S. Social Security Administration, which assumes that mortality rates will continue to decline at the current annual rate, about 0.6 percent, projects that people born in 2030 will have a life expectancy at birth of just over 84 years; those born in 2075, just over 86. If mortality rates decline 2 percent a year, babies born in 2030 could expect to live 104 years; those born in 2075, more than 115 years. But even this rapid rate of decline would have little effect on the U.S. population distribution until past mid-century.

How would rapidly declining mortality affect the U.S. workplace and public programs to support the elderly? Much would depend on the onset of physical decline in the longer-lived Americans. Would greatly increased longevity mean longer periods of dependency? Or would older Americans stay healthy longer? If workers were able to keep working for a greater portion of their lives than they do now, the cost of supporting the elderly might increase only slightly because the ratio of retirees to active workers might increase only a little. If current retirement age patterns persisted, however, the cost of increased longevity would rise sharply as people spent ever more years outside the labor force.

Little in economic theory or empirical evidence suggests that sharply increased longevity would directly affect retirement behavior. But if workers extended their years in retirement, it would boost pension costs, which, in turn, would probably force changes in public policy to encourage workers to extend their working lives. Higher pension costs would necessitate sharply increased pension contributions by workers or their employers, or higher taxes on workers and employers to support public pensions, or cuts in benefits

and increases in the age at which pensions are first paid. These changes would likely cause Americans to work more years than they now do.

Rapidly falling mortality would certainly affect government revenues and spending. If longer-living Americans extended their working lives, they would earn and produce more, swelling tax revenues. But increased longevity would also boost government spending on Social Security, Medicare, and Medicaid, all of which are already projected to grow rapidly as baby boomers begin retiring. And a major new decline in mortality rates would drive spending above these already steeply rising trends.

Social Security costs are officially projected to increase between now and 2080, from just under 11 percent to just over 20 percent of earnings subject to the Social Security payroll tax. If mortality rates were to fall 2 percent annually while the duration of working lives remained the same, Social Security costs would reach more than 25 percent of payroll. Raising the age at which full Social Security benefits are paid by one month a year starting in 2018 would eliminate most of the additional longevity-related cost. The message is simple and clear: as longevity increased, so too would Social Security costs.

Projecting the effects of longevity on Medicare and Medicaid costs is much trickier because spending depends not only on the number of beneficiaries, but also on trends in the cost of medical care. Regardless of trends in mortality rates, Medicare and Medicaid costs will soar because per capita medical costs for everyone will increase. Medical spending also rises with age as people’s bodies gradually wear out or become subject to disease. Some observers see decline as an immutable consequence of a person’s age since birth—an 80-year-old whose life expectancy is 85 will be in the same state of decline as an 80-year-old whose life expectancy is 110. But Stanford University economist John Shoven thinks it more plausible that medical spending depends on years until death. And the fact that disability rates have fallen as mortality rates have improved supports that view. If mortality declines

at historical rates, projections based on the years-since-birth assumption show Medicare costing about 2 percent of gross domestic product more in 2070 than if costs are projected on the years-until-death assumption. The difference jumps to roughly 5 percent of GDP if mortality rates fall 2 percent a year. In the case of Medicaid, the cost difference in 2070 between projections is a bit over 1 percent of GDP if mortality declines at officially assumed rates, but nearly 6 percent if it declines 2 percent a year.

The story is straightforward. Costs of Social Security, Medicare, and Medicaid will rise during the early part of the 21st century, primarily because of the aging of the baby-boom generation and—in the case of the health programs—increases in medical costs. Accelerated increases in longevity would affect costs primarily in the second half of the century and beyond. If, in the best scenario, physical decline were delayed as lives were lengthened, the added health care costs would be modest. If, in addition, working lives increased, the added revenues from a bigger labor force would help defray these costs.

A Global Perspective

The effects of a sharp increase in longevity would not be confined to one nation. The swelling ranks of the elderly already threaten pension systems in many countries and may have important effects on international capital flows. Dramatically increased longevity would require most developed nations to reform their retirement systems to keep them sustainable. Increased public spending on retirement would lower saving rates in developed nations, which could prevent many developing nations from borrowing to finance growth.

Over the past 150 years, both birth and mortality rates have fallen nearly everywhere. From the standpoint of economic development, the ideal pattern is a drop in birth rates followed years later by declining mortality. That pattern keeps the ratio of the working-age population to the total population quite high for a time, enabling domestic saving to support high rates of investment. Eventually, however, the aged

population increases. If birth rates remain low, overall population, excluding immigration, will fall.

Only wealthy nations would be able to afford the costly medical interventions that would sharply increase longevity. Because mortality rates in those nations are already low among younger citizens, declining mortality rates primarily would increase the number of those over age 50. The ratio of the elderly to the working-age population would therefore increase most in wealthy nations. The most extreme effects would show up in nations such as Japan, where the elderly population is already 71 percent as large as the working-age population. The effect in the United States would be much smaller because above-average birth and immigration rates are projected to keep the working-age population growing at least slowly.

Current population aging is already likely to lower both saving and investment in high-income countries and to increase saving in middle-income and poor nations, pushing foreign trade balances of rich nations into deficit and those of the rest of the world into surplus. A 2-percent-a-year reduction in mortality rates would intensify these effects. Saving would decline sharply, investment somewhat less. With mortality falling fastest in nations that can afford medical innovation, trade deficits are especially likely for rich nations.

These projections are tentative and depend heavily on how increasing longevity affects the world of work. If people's working lives lengthen, investment will be higher, the cost of private and public pensions lower. Technological change will also influence investment opportunities and the call on saving to finance that investment. Nevertheless, extending longevity is likely to be quite expensive, and rich nations are far more likely than poor nations to incur those costs.

The Ethical Dilemmas of Increasing Longevity

Throughout the 20th century, public health advances, rising income, and medical discoveries added decades to

life expectancy at birth. These advances raised practical questions, such as how to pay for pension and health costs for the elderly, but relatively few ethical problems did arise: whether it is ever right—and, if so, under what circumstances and after what steps—to curtail care for extremely ill patients or to allow severely damaged newborns to die. But few observers questioned whether clean water, the reduction of poverty, or effective antibiotics were ethically desirable.

The prospect of an engineered extension of human life, however, has created a major stir among ethicists. As Alexander Morgan Capron, University Professor of Law and Medicine at the University of Southern California, notes, past developments in longevity took opportunities once available to the few and extended them to the many. But some interventions now in prospect would change the fundamental character of humans—for example, by changing their genes.

The ethical issues raised by life extension depend in part on its consequences. Most problematic would be increasing the average age of death primarily by increasing a person's years of physical and mental decline. But, as Capron points out, no one can foresee whether the coming scientific advances will add decades of mental and physical vigor or decades of senility and debility.

The ethical issues will also be shaped by the means used to increase longevity. Irreversible interventions, such as altering human genes, raise more questions than do interventions that can be stopped, such as a hormone that a patient can stop taking. And many innovations that promise to extend life will require risky experimentation and must be attended by stringent procedural safeguards.

Another issue is access to life-extending interventions. Capron dismisses the views of some ethicists that once a person has reached a "normal" life span, access to life-extending care is not ethically required. Both the duration of "normal" lives and the content of "normal" interventions, he notes, are

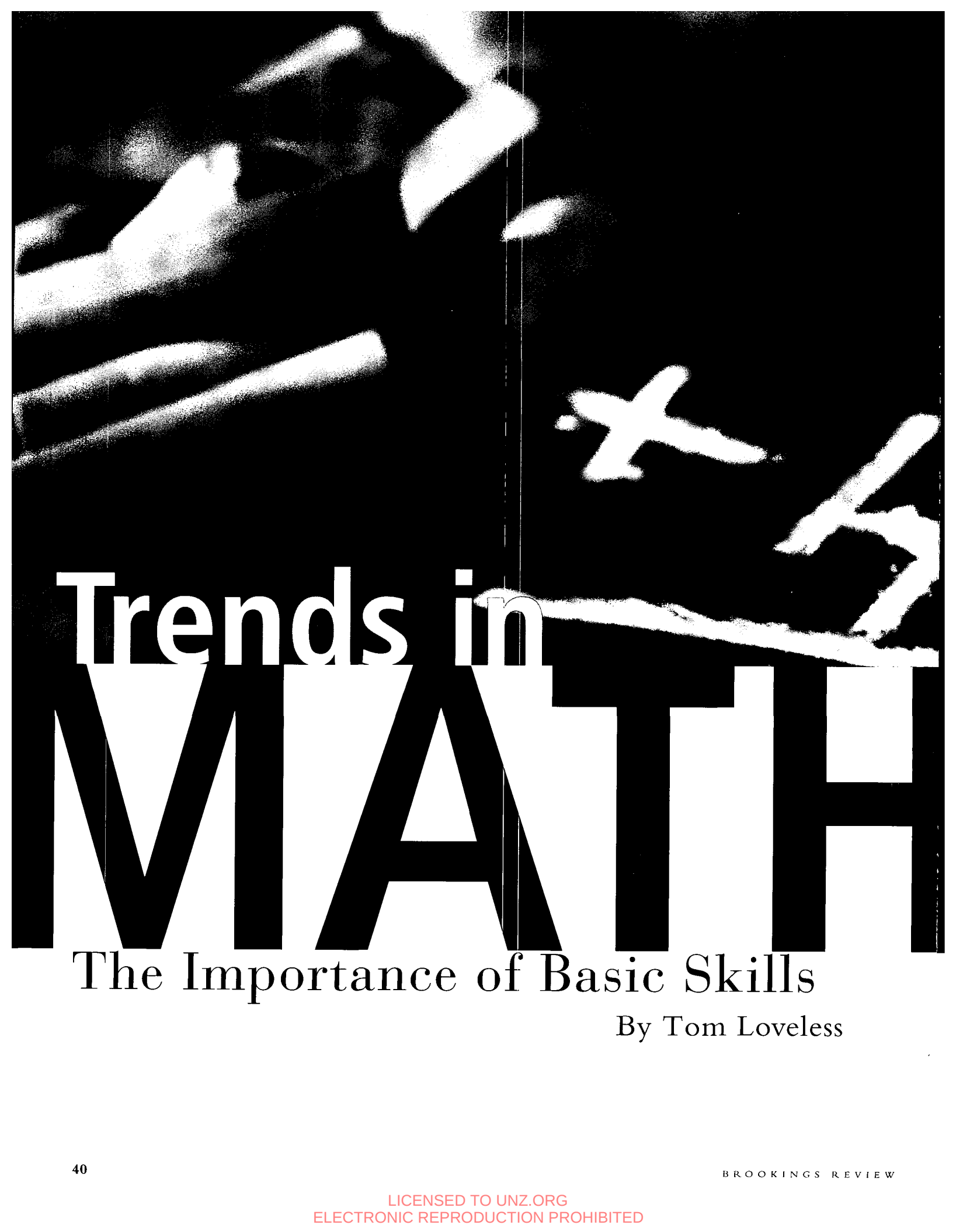
inescapably elastic. Both depend on expectations that are themselves influenced by technological possibilities.

Finally, Capron notes that questions about suicide and passive euthanasia are likely to become increasingly prominent. If the capacity to extend life is available, is it euthanasia if caregivers do not use it—or suicide if patients actively reject it?

Leon Kass, Francis Fukayama, and others have posited that life extension is not a legitimate goal of science and that success in such an endeavor threatens to deprive people of essential attributes of their humanity. Finitude, they argue, lends life savor, sweetness, and value. A quest for superhuman intelligence, looks, or longevity is quite literally inhuman. Gradually, step by step, like the person immersed in a bath slowly warming from comfortable to lethal, humans would surrender what it means to be human by a series of steps each seemingly reasonable, but cumulatively dehumanizing. Capron is more concerned that successful life extension could produce a dystopia with ever-larger parts of life spent in dependence.

When Imagined Futures Become Real

A flowering of biomedical science holds the promise, though not the certainty, that human beings will soon live routinely to ages almost unthinkable today. Although such a development still has an air of science fiction for most Americans, its implications must be considered seriously. Authors of fiction tend to place utopias and dystopias in an imagined future. Readers may be revulsed by the nightmares of *Brave New World* or *1984*, chilled by the cold impersonality of *The Rise of the Meritocracy*, or swept by the romantic notions of *Looking Backward*. The authors of these imagined futures had a free hand to paint with their chosen palettes. Social scientists, having no such license, must contemplate with academic detachment the problems, challenges, and opportunities to be faced if living to 90, 100, or beyond becomes common. Utopias do not adorn the pages of honest analysis. ■

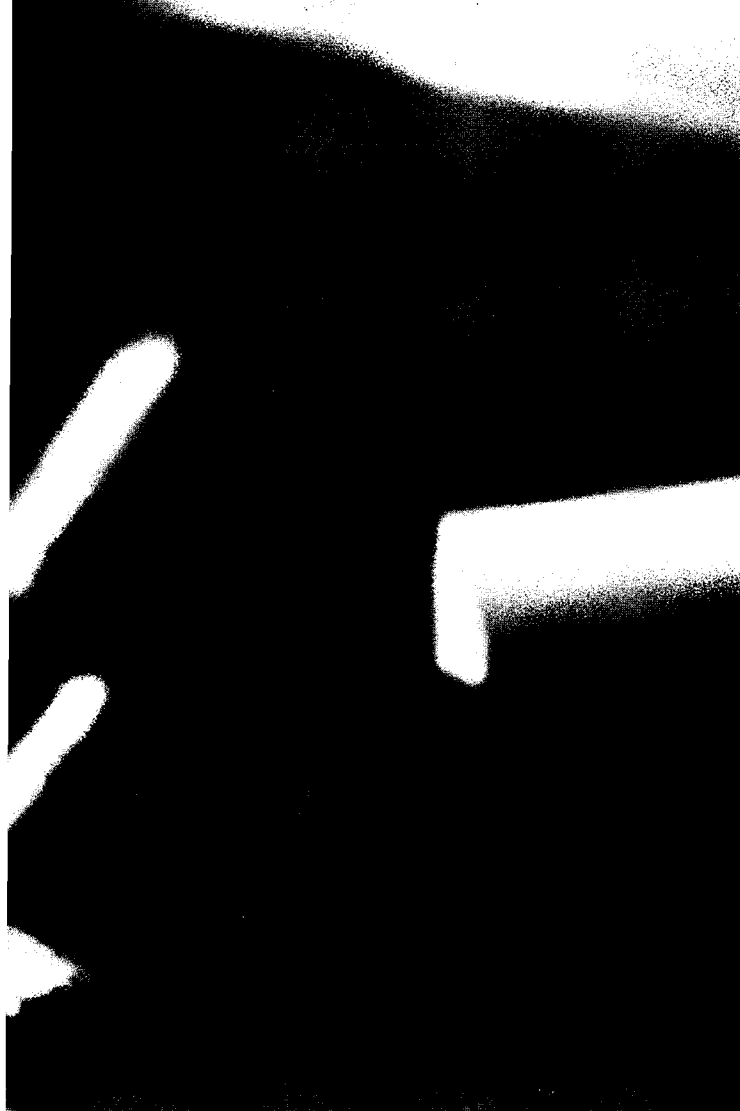


Trends in

MATH

The Importance of Basic Skills

By Tom Loveless



argue that students no longer need to learn how to compute now that calculators are widely available. The truth is that, calculators or no calculators, basic math skills are still important. Unless every student receives a thorough grounding in arithmetic, the nation has little chance of achieving ambitious goals in mathematics.

Let's look at some data.

Main and Trend

The NAEP administers two math tests, the main and the long-term trend. The main NAEP test has been given since 1990. Its questions may be changed slightly from test to test, but the test faithfully reflects the goals of the National Council of Teachers of Mathematics. As shown in figure 1, main NAEP scores have increased significantly—scores for twelfth, eighth, and fourth grades are all up.

Figure 1.
Main NAEP, 1990–2000

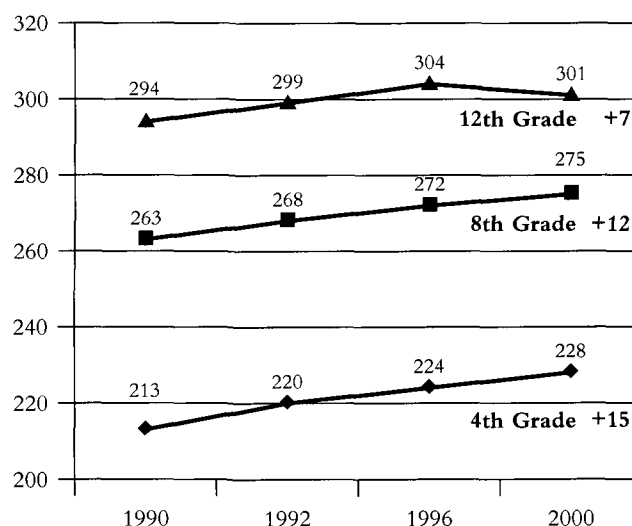
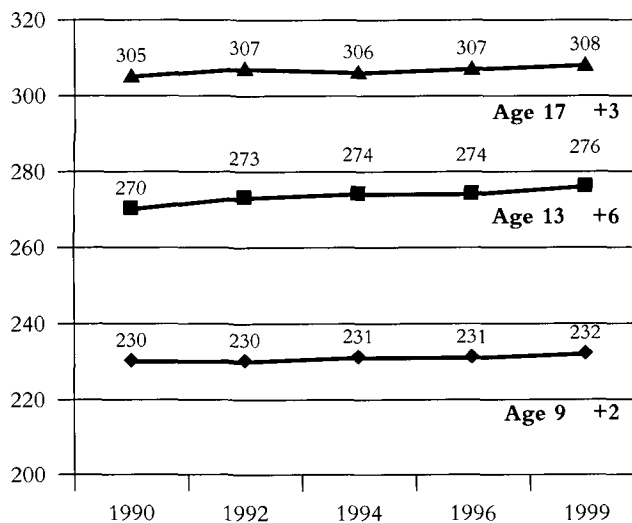


Figure 2.
Long-term Trend NAEP, 1990–99



How are American students doing in mathematics? Trends on the two math tests of the National Assessment of Educational Progress (NAEP) show that although students have made progress in some areas of math, improvement has been disappointing when it comes to basic arithmetic—in particular, the ability to compute. In recent years, in fact, progress has ground to a halt.

Is this new slowing of progress in basic math a matter for concern, especially if American youngsters are showing gains in more sophisticated areas of math? After all, some people

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Figure 2 shows scores on the trend NAEP, whose questions have remained the same throughout the life of NAEP. Since 1990, scores are up, but not as much as on the main NAEP. For ease of comparison, table 1 converts the two tests' gains and displays them in standard deviations, a unit of measure used by statisticians. Gains on the main NAEP are at least twice as large as those registered on the trend. The difference between the two tests is most apparent with the youngest students, 9-year-old fourth graders. They accomplished a huge gain on the main NAEP, 0.29 standard deviations, equal to about 1.2 year's worth of mathematics. But on the trend NAEP, the gain was minuscule, equal to about one month of learning.

Table 1.
Main NAEP and Trend NAEP Math Gains in the 1990s
Standard deviation units

		MAIN 1990-2000	TREND 1990-99
Grade 12	Age 17	+0.14	+0.05
Grade 8	Age 13	+0.16	+0.08
Grade 4	Age 9	+0.29	+0.03

Why are the two tests telling completely different stories? The most likely reason is that they assess different skills. The main NAEP devotes more items to measuring students' skills in areas such as geometry, problem solving, and data analysis. For assessing basic skills, and especially for measuring computation skills, the trend NAEP is the better test. As the NAEP framework states, the trend test is the one that can "provide insight into students' computational abilities."

With that in mind, some Brookings colleagues and I identified computation items on the trend NAEP, grouped them by topic, and calculated gains for both the 1980s and the 1990s. It is important to note that the analyses are based on a small number of NAEP items. Though this is the best available evidence on computation skills at the national level, the findings are not conclusive but merely suggestive. That said, the findings pinpoint important areas where problems may be developing.

Computation

Table 2 breaks down computation scores into 10 separate areas of skill. The percentage of students answering items correctly is presented for 1982, 1990, and 1999. The last two columns compare gains or losses in the 1980s and 1990s, with the better performing decade being shaded. Overall, students gained more in computation during the 1980s than during the 1990s, with eight of the ten clusters favoring the 1980s, two favoring the 1990s. In the 1990s column, most cells are negative, showing that students lost ground in most computation skills during the 1990s. Only in computing percentages at ages 13 and 17 did students register gains.

Take a closer look at the scores for 9-year-olds. These skills comprise the basic arithmetic that all fourth graders are

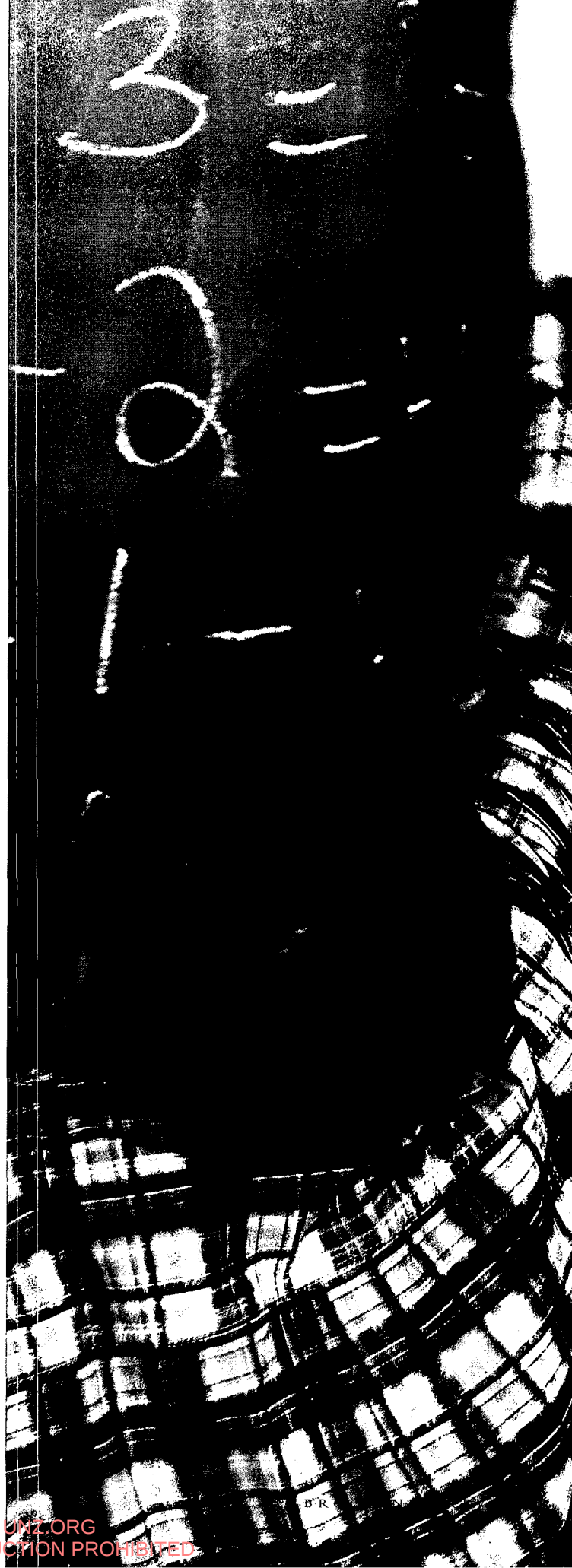


Table 2.
Trends in Computation Skills, NAEP, 1982–99

	SKILL CLUSTER (NUMBER OF ITEMS)	1982	1990	1999	CHANGE 1982–90	CHANGE 1990–99
Age 9	Addition (4)	71.4	75.7	75.5	4.3	-0.2
	Subtraction (3)	53.4	63.4	59.7	10.0	-3.7
	Multiplication (2)	37.4	43.9	42.5	6.5	-1.4
	Division (2)	44.3	49.1	48.3	4.8	-0.8
Age 13	Whole Numbers (9)	92.7	91.4	89.5	-1.3	-1.9
	Fractions (4)	59.7	56.8	54.3	-2.9	-2.5
	Percentages (6)	39.1	38.8	46.7	-0.3	7.9
Age 17	Fractions (3)	66.9	75.8	55.5	8.9	-20.3
	Decimals (3)	51.3	50.4	46.3	-0.9	-4.1
	Percentages (6)	56.3	66.5	70.0	10.2	3.5

expected to master—addition, subtraction, multiplication, and division of whole numbers. All four areas reversed direction in the 1990s, turning solid gains made in the 1980s into losses. Not only that, but the declines came from levels that weren't very high at the beginning of the 1990s—certainly not at a level that is acceptable for such fundamental material.

I taught sixth grade for several years in California. My grading scale for tests and quizzes was pretty straightforward: 90s were “A’s,” 80s were “B’s,” 70s were “C’s,” 60s were “D’s,” and below 60 percent was an “F.” The 1999 NAEP scores for 9-year-olds would have received the following letter grades in my class: a “C” in addition, a “D” in subtraction (with the benefit of rounding), an “F” in multiplication, and an “F” in division. Those are not good grades. Think of it this way. Youngsters who have not mastered whole-number arithmetic by the end of fourth grade are at risk of later becoming remedial students in mathematics. Half of the nation’s 9-year-olds missed the multiplication and division items on the trend NAEP the last time the test was given.

The proficiency of 13- and 17-year-olds on computation skills also remains unacceptably low. Although proficiency with fractions is critical in preparation for algebra, in 1999 only about half of 13- and 17-year-olds could compute accurately with fractions on the NAEP. Students who leave eighth grade not knowing how to compute with fractions enter high school as remedial math students. Students who leave high school lacking proficiency with fractions are inadequately prepared for college mathematics. On the most recent trend NAEP, both age groups were less proficient at computing with fractions than their peers were in 1982, more than 20 years ago.

Should we be worried if the evidence suggests that students are not learning how to compute? We should—for three reasons. First, basic skills serve equity. As shown in table 3, the lack of progress in computation skills has disproportionately affected African-American students. The black-white achievement gap expanded in every computation skill area in the 1990s. This is typical of what happens when basic skills are shortchanged. When basic skills are not taught, the least privileged in our society—those who cannot afford tutors, sophisti-

Table 3.
Change in Computation Skills, NAEP, by Race, 1990–99

	SKILL CLUSTER (NUMBER OF ITEMS)	WHITE	BLACK	BLACK-WHITE GAP*
Age 9	Addition (4)	-0.2	-0.5	0.3
	Subtraction (3)	-2.4	-8.1	5.7
	Multiplication (2)	-1.2	-3.6	2.5
	Division (2)	-0.1	-6.0	6.0
Age 13	Whole Numbers (9)	-1.6	-4.7	3.1
	Fractions (4)	-2.1	-4.0	1.8
	Percentages (6)	9.0	3.8	5.1
Age 17	Fractions (3)	-17.8	-33.6	15.8
	Decimals (3)	-1.9	-13.1	11.2
	Percentages (6)	5.9	-3.4	9.2

* May not be reflected in table because of rounding

cated computer programs, or academic summer camps—suffer the biggest losses. The students who pay the biggest price are those who can least afford it. Unfortunately, they are also students for whom the educational system has never worked well.

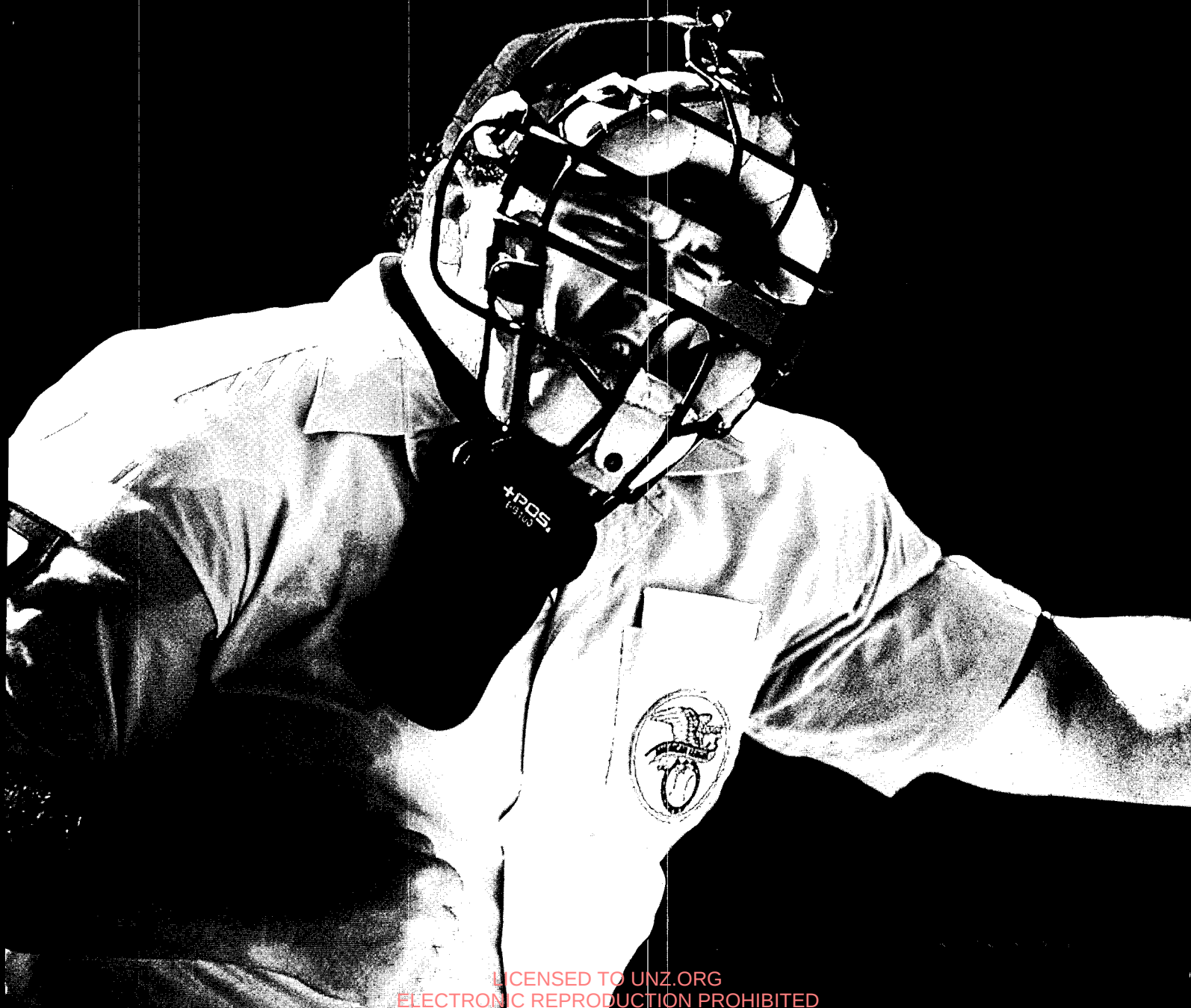
Second, basic skills are necessary to advance in math. Insisting that students master computation skills is not to advocate that they stop at the basics. Basic skills are a floor, not a ceiling. Students must learn arithmetic so that they can move on to more demanding mathematics—algebra, geometry, calculus. An emphasis on the basics should never be used as an excuse to straitjacket students or to slow their progress in the math curriculum.

And finally, basic skills predict adult earnings. In recent years, a growing body of research has documented that the skills and knowledge students learn in school is correlated with success later in life. In their landmark study showing the impact of basic skills on adult earnings, Richard Murnane and Frank Levy conclude, “Mastery of skills taught in American schools no later than the eighth grade is an increasingly important determinant of subsequent wages.”

Forward to Basics

About one-half of U.S. 9-year-olds cannot multiply or divide whole numbers accurately, and half of 13- and 17-year-olds cannot compute correctly with fractions. These deficiencies mean that large numbers of American elementary students are ill prepared to study algebra in middle school, large numbers of middle school students are inadequately prepared to take advanced mathematics courses in high school, and large numbers of high school students have not mastered the rudimentary skills required for entering college or gaining middle-class employment. A 50 percent proficiency rate is unacceptable. But it does not justify a call for “back to basics.” Back to basics implies some past golden age when everyone learned essential skills. That age never existed. To ensure that every American student is proficient at basic math skills mandates that the nation go forward, not backward. The goal of leaving no child behind is nothing but a pipe dream if children don’t learn arithmetic, the starting point in mathematics. ■

Win



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The World Series of October 2001 between the Arizona Diamondbacks and the New York Yankees was more than just scintillating baseball. In that seven-game series, America's pastime became a healing ritual, and baseball helped bring the nation together after the shocking terror attacks of September 11. But the world of baseball was not what it may have seemed during that brief interval. Much was—and is still—amiss.

Just one month after the 2001 World Series ended, baseball commissioner Bud Selig went before Congress to plead poverty for his industry. To get its economic house in order, Major League Baseball proposed to eliminate two or more teams—at the same time that several potential host cities,

exemption has been linked to its player reserve system, which for almost a century gave a team sole rights over a player and forbade players to solicit competitive bids for their services. In 1976, however, a collective-bargaining agreement between Major League Baseball and the Players Association ended that reserve system, lifting the reserve clause from players with six years of major league experience and instituting a system of limited “free agency.” And in 1998 Congress passed legislation that lifted baseball's antitrust exemption as applied to labor relations. But even though the reserve system has been in history's dustbin for more than a quarter-century, the antitrust exemption itself remains—though its convoluted history is one for the books.

The exemption is founded in the 1922 *Federal Baseball* case. In *Federal Baseball* the Supreme Court affirmed a U.S. District of Columbia Court of Appeals ruling that baseball was a sport, not interstate commerce—and thus not subject to the Sherman Antitrust Act. In 1948 the Second Circuit Court of Appeals, calling the reserve clause “shockingly repugnant to moral principles...that have been basic in America...[since] the Thirteenth Amendment...condemning ‘involuntary servitude,’” ruled that baseball was subject to antitrust law. But the Circuit Court suit was settled out of court before the Supreme Court could rule on appeal—and thus was born the ambiguity about whether baseball is subject to antitrust. That same ambiguity explains why the antitrust exemption is often referred to as baseball's “presumed” antitrust exemption.

In 1951, Major League Baseball requested Congress to affirm its exemption. The House Subcommittee on the Study of Monopoly Power held protracted hearings on the subject but passed no legislation. Many observers believe that the House committee thought that the 1948 ruling had superseded the 1922 ruling and that the failure to pass new legislation to grant MLB an exemption meant that the sport would be subject to the nation's antitrust laws.

Yet, in 1953, the Supreme Court reaffirmed the 1922 decision and handed the ball back to Congress, observing that “in *Federal Baseball*...this Court held that...professional baseball...was not within the scope of the federal antitrust laws. Congress had the ruling under consideration but has not seen fit to bring such business under these laws by legislation....We think that if there are evils in this field which now warrant application to it of the antitrust laws it should be done by legislation.”

Baseball's exemption became still more anomalous in 1957 when the Supreme Court ruled, in *Radovich v. NFL*, that the National Football League is subject to antitrust statutes. And in 1972 (in *Flood v. Kuhn et al.*) the Court once more affirmed the 1922 decision while calling it an “aberration” and an “anomaly”—prompting the *New York Times* to opine, “The Supreme Court made a mistake the first time it considered the subject 50 years ago and now feels obliged to keep on making the same mistake because Congress does not act to repeal the exemption it never ordered.”

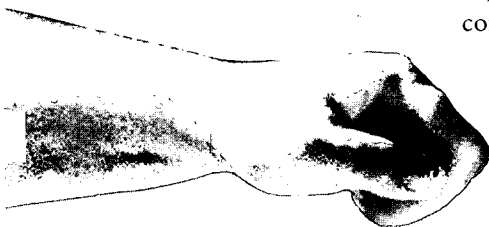
Since 1990 several judicial rulings on the status of baseball's exemption have resolved little. One state ruling and one fed-

COMPETITIVE

including the nation's capital, were begging for a major league team. Meanwhile, various team owners were demanding public subsidies from their host cities for new stadiums—and threatening to move their teams if the subventions were not forthcoming. High-revenue teams such as the Yankees maintained their dominance over low-revenue teams, and threats of another player strike sapped fan interest. Ticket prices climbed ever higher, and attendance continued to fall, with 20 of the 30 major league teams dropping at the gate in 2002. Overall, attendance fell 6 percent in 2002 and, as of the All-Star break, attendance was down another 5 percent in 2003.

These recurrent problems are all related to baseball's special status as an unregulated legal monopoly. Alone among team sports, Major League Baseball enjoys a presumed exemption from the nation's antitrust laws. It is the only top-level professional baseball enterprise in the country, and each of its teams is assigned an exclusive territory (in a few megacities the territory is shared by two teams). Until 1992 the industry claimed that its “independent” commissioner would guard against abuses of baseball's market power and privilege. But the few commissioners who ever consistently behaved independently of the owners' wishes were usually dispensed with in short order by unappreciative owners. And even the illusion of independence was shattered in 1992 when Bud Selig, owner

of the Milwaukee Brewers, was appointed acting commissioner—and then full commissioner in 1998.



The Antitrust Exemption Baseball's antitrust

Andrew Zimbalist is Robert A. Woods Professor of Economics at Smith College and author of *May the Best Team Win: Baseball Economics and Public Policy* (Brookings, 2003), from which this article is drawn.

eral ruling have held that the exemption applies narrowly to baseball's (now defunct) reserve clause and to no other aspects of the industry. One state and two federal rulings have held that it applies broadly to the entire business of baseball. Together the rulings cover only three of the eleven judicial circuits in the United States, leaving ample ambiguity in the status of the scope of the exemption in the remaining circuits.

Baseball's Ups and Downs

Despite the lingering presumed antitrust exemption, the fortunes of baseball (and its competitive balance) steadily improved between 1965 and the end of the 1980s, aided by the demise of the reserve system and by a reverse-order amateur draft in which teams with the worst records choose first. Before free agency, when players were stuck with a team for their whole careers unless they were traded or released, big-city owners bought good players from small-city owners. The extra revenue produced by these top players went to the owners, not the players, and high-revenue teams disproportionately accumulated player talent. The free-agent market allowed weak teams to improve themselves rapidly and made it more difficult for winning teams to hold together. Competitive balance improved and the era of team dynasties seemed to be gone forever.

Then came the 1990s. Baseball's 1990–93 national television contract with CBS and ESPN awarded each team roughly \$19 million a year—almost 40 percent of the average team revenue—from baseball's central coffers to help equalize team strength and keep baseball competitive. But the value of the new 1994 TV contract fell more than 60 percent. With centrally distributed monies falling below \$8 million per club, big-market teams like the Yankees and teams like the Baltimore Orioles with new, big-revenue-generating stadiums found their revenue edge growing rapidly.

The revenue disparity between the richest and poorest teams grew from around \$30 million in 1989 to \$208 million in 2001. As franchise values rapidly escalated, owners increasingly had to be extraordinarily wealthy individuals or corporations that frequently owned other businesses with ties to the baseball teams. In 2001 the Anaheim Angels, Atlanta Braves, Toronto Blue Jays, Chicago Cubs, Los Angeles Dodgers, Cleveland Indians, and Texas Rangers were owned by media companies or media moguls. And the Yankees, Boston Red Sox, and Philadelphia Phillies either owned media companies outright or had joint ventures with them. The baseball teams themselves were only small cogs in large enterprises, but teams like the Yankees and the Braves—inundated with revenue from many sources—grew into dynasties that smaller, low-revenue franchises could not hope to match.

Although baseball has seen and survived past dynasties, such as the storied Yankee teams of the 1950s and early 1960s, the game today is more vulnerable than it was half a century ago. Teams that perform poorly year after year and have few prospects for becoming competitive risk losing fans for good. The game's core base of fans is aging, and younger audiences are enticed by a growing list of professional sports and entertainment options.

Meanwhile, the problem of real and threatened franchise movement continues. Baseball's monopoly allows it to restrict artificially the number of franchises and to dally with cities that have no team—to hold out to them the elusive promise of a franchise, pressuring existing host cities to build new stadiums or otherwise do MLB's bidding. As a consequence, cities and states compete against each other, leading to exorbitant stadium-financing packages and sweetheart leases. Cities have attempted on their own to include lease provisions that deter team relocation and provide a more equitable sharing of the facility returns. But usually only the largest cities have sufficient bargaining leverage to accomplish even part of these aims.

Moreover, baseball's insulation from competition has also contributed to a lax and inefficient management culture. Consider the World Series you are about to watch. Home field advantage this year for the first time was decided by the winner of this year's All-Star Game. Why? Not because it made any logical or competitive sense, but because baseball was desperately grasping for a way to boost its flagging ratings for the mid-season classic. (Despite this artificial inflation, the 2003 All-Star Game failed to improve its television ratings and even saw its ratings fall 9.7 percent in the key 18–34 male demographic relative to its record-low ratings in 2002.) The pattern here is well established. Grab for the proximate dollar and never mind about the long-term consequences.

Or consider the revealing message in Michael Lewis's new book *Moneyball: The Art of Winning an Unfair Game*. For decades, baseball teams' front offices were run by "good old boys" who followed a dubious lore of player evaluation as if it were catechism. The enlightening statistical analyses of the game by innovators like Bill James went ignored until Sandy Alderson in Oakland decided that his team could benefit from James's insights in the mid-1990s. And benefit they did, creating a first-class competitive team on a shoestring budget. Now, after a 25-year delay, several teams are beginning to change their ways and introduce the teachings of Bill James and his followers.

Or take the absence of a Major League Baseball team in our nation's capital, the eighth-largest media market. The National Football League, the National Basketball Association, and the National Hockey League, all without antitrust exemptions, have teams in Washington, D.C., but not Major League Baseball.

Baseball may finally have mismanaged itself into a position where Congress may be willing to enact some meaningful public policy reforms to curtail MLB's monopoly powers. Congressional initiatives in this area, however, would have to rise above a history plagued by local chauvinism and myopia. In the past, sponsors of legislation have invariably reacted to a team movement problem in their state or district, opportunistically seizing the occasion to posture in defense of their constituents. While it is arguable that there could be a small gain in net global welfare when a team relocates from a smaller to a larger city, it is clear that proper public policy should be oriented toward increasing the supply of baseball franchises so

that all economically viable cities have a team. In this as in other problem areas, the solution is to strip MLB of its antitrust exemption, exposing it to judicial review and additional competitive pressure.

Solving the Problem

In a 1972 decision involving the reserve clause, the chief justice of the Supreme Court stated, "It is time the Congress acted to solve the [antitrust exemption] problem." Nothing has transpired in the ensuing 30 years to lessen the urgency of that appeal.

But even if Congress were to resolve the ambiguity over the scope of baseball's presumed exemption in favor of judicial review and competition, lifting the exemption would not guarantee competition in the industry. It would merely potentially put a check on restrictive behavior—and encourage much-needed judicial discovery of facts and analytical challenge of baseball's assertions. To promote competition and resolve the problems noted above, Congress should contemplate a forced divestiture of MLB into two competing business entities. The entities would be allowed to collaborate on playing rules and on interleague and postseason play, but not to divide up metropolitan areas, establish common drafts or players' markets, or collude on broadcasting policy. Under these circumstances neither league would be inclined to vacate an economically viable city, and, if it did, the competing league would be likely to jump in, just as McDonald's and Burger King rush to beat the other to any viable strip mall. Other consumer-friendly consequences would flow from such an arrangement, and lower local, state, and federal subsidies would scale down team revenues, owner profits, and player salaries. But competition would compel more efficient management practices and teams would remain solvent, albeit with reduced cost structures.

When he was still baseball commissioner, Fay Vincent referred to Washington, D.C., as an "asset" of baseball even though no team was playing in the nation's capital. Why? Because D.C. was and is a potential host of a team and could be used to leverage better deals from other cities. Baseball treated D.C., in a sense, as if it owned the town. This sense of ownership, in turn, derives from the artificial scarcity of franchises that baseball enforces as a monopolist. Were there two competing major leagues, Washington would have one franchise, or perhaps two, in a heartbeat.

With two competing baseball leagues, most, if not all, of MLB's competitive-balance issues would be resolved. Not only would cities now bereft of baseball find themselves host-

ing teams, but some host cities might find an additional team or two in their market. If sharing the New York City market with the two existing teams offered better prospects for a franchise than, say, having New Orleans to itself, New York City might once again have three (or more) baseball teams. If the Yankees and Mets had to share New York with additional teams, much of their competitive advantage over smaller markets would disappear. Indeed, with competition over time one would expect teams to allocate themselves across the country so as to equalize the expected incremental revenue from each venue.

One potential downside to divestiture is that competition between two leagues will tend over time to result in one league growing stronger and the other weaker. The weaker league may see some of its franchises fail and may eventually be absorbed by the stronger league. The result would first be instability, followed by the possible reassertion of monopoly.

This possibility, however, seems both remediable (divestiture could be legislated again in the future) and a modest price to pay given the expected benefits of competition.

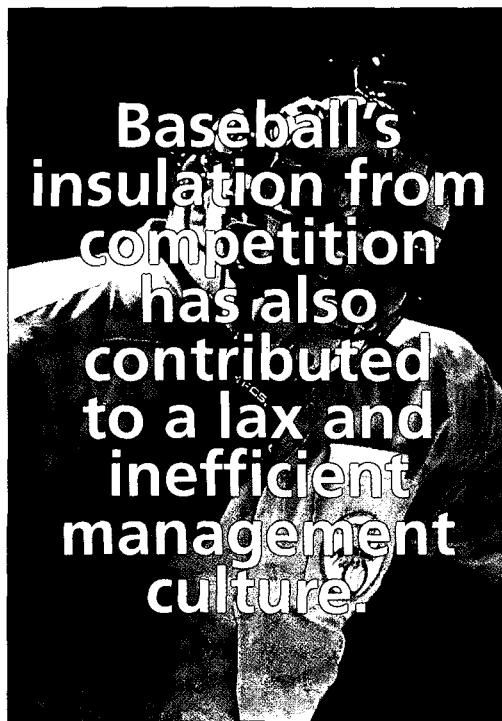
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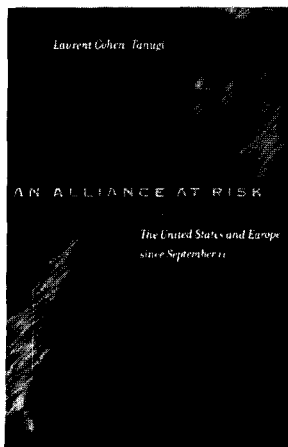
The U.S. House of Representatives and Senate have been prompted to consider public policy remedies for baseball more than 60 times since 1950, 16 times since 1990. Congress has never acted either to regulate or to break up MLB. With one minor exception, it has also never acted to take away baseball's presumed antitrust exemption.

It is useful to remember that in the past, rational public policy toward baseball has been impeded by "rational politics"—that is, politics where politicians act in their own best interest. As sports franchises have skyrocketed in value, today's owners tend to

be some of America's wealthiest and most powerful individuals and corporations. As such, baseball ownership has important and close ties to members of Congress and, needless to say, to the man in the Oval Office. Congressional reluctance to curtail MLB's monopoly powers is hardly surprising.

But while most baseball issues taken up by Congress over the years have been local in nature, baseball sometimes seems to do its best to agitate the whole country at once. The announced intention of the owners to eliminate at least two teams along with their minor league affiliates out of a dozen or so contraction candidates in 2001 (now postponed until 2006) may arouse enough members of Congress to undo the historical record of inaction. There is no reason for public policymakers to sit back and hope that baseball's barons will finally get it right. ■





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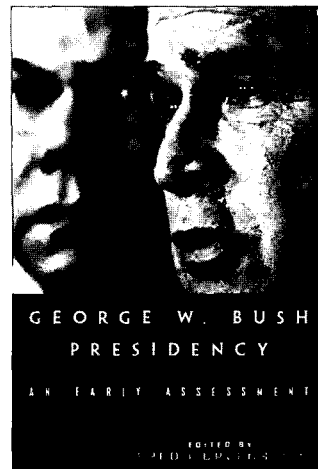
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